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No. 12471

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**United States  
Court of Appeals**  
for the Ninth Circuit.

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SAM SCHNITZER,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

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**Transcript of Record**

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**Petition to Review a Decision of the Tax Court  
of the United States**

**FILED**

APR 5 1950

**PAUL P. O'BRIEN,**  
CLERK





No. 12471

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United States  
Court of Appeals  
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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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The Tax Court of the United States

T. C. Docket No. 14208

SAM SCHNITZER,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

### PETITION

The above named petitioner hereby petitions the above entitled court for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his Notice of Deficiency (Bureau Symbols IT:90D:DLA) dated March 3, 1947, and as a basis of his proceeding alleges as follows:

#### I.

The petitioner is an individual residing at 1011 S. W. Vista Avenue, Portland 4, Oregon. The returns for the periods here involved were filed with the Collector for District of Oregon. The petitioner made and executed said returns as S. Schnitzer and said Notice of Deficiency was addressed to him as S. Schnitzer for the reason he ordinarily uses only his initials in the transaction of business.

#### II.

The Notice of Deficiency (a copy of which is attached and marked Exhibit A) was mailed to the



petitioner from Seattle, Washington, under date of March 3, 1947.

### III.

The taxes in controversy are income taxes for the calendar years 1942 and 1943 and in the amount of \$151,044.45.

### IV.

The Determination of the tax set forth in said Notice of Deficiency is based upon the following errors:

(a) The Commissioner erred in refusing to recognize that Rose Schnitzer was a partner in The Alaska Junk Company during the calendar years 1942 and 1943 with an interest therein equal to that of the petitioner.

(b) The Commissioner erred in including an additional \$54,030.86 in petitioner's income for the calendar year 1942 as a result of his refusal to recognize Rose Schnitzer as a partner in The Alaska Junk Company.

(c) The Commissioner erred in disallowing as a deduction of The Alaska Junk Company in the calendar year 1943, the sum of \$202,350.60 as (1) a bad debt owed to The Alaska Junk Company by the Oregon Electric Steel Rolling Mills which became worthless in said calendar year, or (2) a loss deductible under the provisions of Sec. 23 (e), IRC.

(d) The Commissioner erred in including an additional \$157,689.23 in petitioner's Income Tax

Net Income and in his Victory Tax Net Income for the calendar year 1943 as a result of his refusal to recognize the said Rose Schnitzer as a partner in the Alaska Junk Company and his said disallowance of the said sum of \$202,350.60 as a deduction of The Alaska Junk Company. (The refusal to recognize the said partnership interest of Rose Schnitzer having the effect of increasing petitioner's said income for said calendar year by the sum of \$56,513.93, and his disallowance of the said deduction having the effect of increasing his said income for said calendar year by the sum of \$101,175.30.)

## V.

The facts upon which the petitioner relies as the basis of this proceeding are as follows:

### Re Partnership

(a) At and during the calendar years 1942 and 1943, and for a great many years prior thereto, the petitioner, Rose Schnitzer, Harry J. Wolf and Jennie Wolf were co-partners under the names and styles of The Alaska Junk Company and Schnitzer-Wolf Machinery Company, and as such co-partners were engaged in the business of buying, selling and generally dealing in junk, new and second hand pipe, tools, machinery, hardware, metal and metal products of every character, and in the business activities hereinafter mentioned, and the principal place of business of said partners was in Portland, Oregon. During all said times each of the said

persons owned a one-quarter interest in the business and property of said partnership.

(b) The Commissioner refused to recognize that Rose Schnitzer and Jennie Wolf were partners in the said business in the calendar years 1942 and 1943 although he had recognized them as such partners for many years prior thereto, and their interests and shares in said partnership were exactly the same in the calendar years 1942 and 1943 as their interest and shares therein throughout all the years in which the Commissioner did recognize and treat them as partners in said partnership.

(c) The petitioner and Rose Schnitzer were intermarried in Portland, Oregon, in 1906 and now are and ever since have been husband and wife.

(d) When the petitioner was married he was 26 years of age, had been in the United States about two years, did not speak English well, for about 9 months prior to his marriage, had been engaged in Portland, Oregon, in the business of buying and selling junk, and had a net worth of approximately \$500.00.

(e) Sometime late in the year 1911 the petitioner and Harry J. Wolf engaged in a joint venture in purchasing and disposing of some salvage material being removed from the Portland Hotel. This joint venture led to the formation of The Alaska Junk Company.

(f) On February 3, 1912, the petitioner, Harry J. Wolf, and one Sam Horwitz caused the Alaska

Junk Company to be organized as a corporation under the laws of the State of Oregon with a capital stock of \$5,000.00 divided into five shares of a par value of \$1,000.00 each, and petitioner transferred to said corporation a stock of junk and second hand merchandise of a reasonable value of \$1,000.00 in payment for one share of capital of said corporation, and Harry J. Wolf transferred junk and second hand merchandise of an equal reasonable value for one share of said capital stock. Sam Horwitz subscribed for but did not completely pay for one share of the capital stock in said corporation. The petitioner and Harry J. Wolf, each paying equal amounts, purchased the interest of Sam Horwitz in said share of capital stock to which he had subscribed.

(g) On April 12, 1912, said corporation was duly dissolved pursuant to a resolution adopted on March 26, 1912, by its board of directors, and its assets were taken over by the petitioner and Harry J. Wolf, with equal interest therein, and thereupon they entered into an oral partnership agreement pursuant to which they became partners with equal interests, under the name and style of The Alaska Junk Company, for the purpose of engaging in the business of buying, selling and generally dealing in junk, pipe and new and second hand tools, hardware, metal and metal goods of every character.

(h) Rose Schnitzer helped Sam Schnitzer accumulate the money with which he purchased the



junk and second hand merchandise transferred to said corporation for his share of the said capital stock and which he contributed for the said purchase of said interest of Sam Horwitz in the capital stock of said corporation.

(i) When the partnership last mentioned was organized the petitioner and Harry J. Wolf each entered into an agreement with their respective wives whereby the interest of each said wife in said partnership was recognized and fixed as being equal to that of her husband, and whereby it was agreed that each said wife should continue to aid and assist in accumulating money to be retained in the business as capital.

(j) The said partnership business was continuously carried on pursuant to the agreements set forth in paragraphs V (g) and (i) until January 3, 1928, when it was decided by the petitioner, Rose Schnitzer, Harry J. Wolf and Jennie Wolf that they would enter into a formal written partnership agreement, and on the date last mentioned said persons did enter into such an agreement whereby it is provided that the interest of each of the said persons in said partnership should be an equal undivided one-quarter interest and that each of them should be entitled to share equally in the profits and losses of the business, that the partners should be allowed to draw wages for their services out of the partnership business, which wages should be



considered as a business expense, and that after deducting all business expenses, including wages paid to petitioner and said Harry J. Wolf, the net profits, if any, should be divided into four equal portions and paid to each of the said co-partners, and the losses, if any, should likewise be borne equally.

(k) That said written partnership agreement from the date it was executed, as aforesaid, remained in force and effect to and including the calendar years 1942 and 1943.

(l) Although said written partnership agreement was not executed until said 3rd day of January, 1928, all of the said parties thereto on many occasions from 1912 to the date of said partnership articles reaffirmed their original agreements mentioned in paragraph V (i), and pursuant to said original agreements said wives continued to assist the petitioner and Harry J. Wolf in accumulating money to be retained in the said business as capital.

(m) During the calendar years 1942 and 1943 and for many years prior thereto the petitioner and Harry J. Wolf drew salaries from said partnership and the same were deducted as business expenses of the partnership prior to any division of the remaining profits by the partners and said salaries were in compensation to the petitioner and Harry J. Wolf for their personal services rendered to the said partnership.

### Re Bad Debt Loss

(n) At and during all the times hereinafter mentioned the Oregon Electric Steel Rolling Mills, hereinafter called the corporation, was a corporation having an authorized capital stock of 2500 shares consisting of common stock of a par value of \$100.00 each, and the petitioner and Harry J. Wolf each subscribed to a portion of the capital stock, which portion was subsequently issued and thereupon immediately reissued so as to divide it equally among the petitioner, Rose Schnitzer, Harry J. Wolf and Jennie Wolf. Thereafter additional stock was issued in substantially equal amounts to each of the four persons last mentioned. Said corporation was fully paid for all said stock. The balance of the issued stock of said corporation was owned by other persons, Morris Schnitzer, son of the petitioner and Rose Schnitzer, owned all of the said balance except three shares.

(o) The said partnership composed of the petitioner, Rose Schnitzer, Harry J. Wolf and Jennie Wolf is hereinafter referred to as The Alaska Junk Company. Said Morris Schnitzer at and during all times hereinafter mentioned was engaged in Portland, Oregon, in the business of buying and selling new and used iron, steel, tools and machinery and conducted such business under the name and style of the Schnitzer Steel Products Co.

(p) In addition to the business activities mentioned in Paragraph V (a), The Alaska Junk Company during 1942 and 1943 and for many years

prior thereto was engaged in the business of promoting and financing business enterprises of a nature related to the activities of said partnership enumerated in paragraph V (a).

(q) In the course of its business The Alaska Junk Company between October 22, 1941, and November 22, 1943, on an open account, at the instance and request of said corporation, advanced money to said corporation, either directly or by making payments on its account to its creditors, purchased and furnished it with merchandise charging the cost thereof to it, and sold goods, wares and merchandise to it at the regular prices charged by The Alaska Junk Company to the trade in general. On November 26, 1943, the balance due and owing to The Alaska Junk Company from said corporation on said open account was \$428,132.13.

(r) In consideration of said open account being credited with the sum of \$174,000.00, the said corporation made, executed and delivered to The Alaska Junk Company 174 First Debentures (unsecured) in the total amount of \$174,000.00, bearing interest at 8% per annum, and on July 14, 1943, said Alaska Junk Company credited said open account with said amount of \$174,000.00, and charged its "Stocks and Bonds" account with a like sum. For a valuable consideration, seventy-five (75) such debentures in the sum of \$75,000.00 were also executed and delivered by said corporation to Morris Schnitzer. No payments of either principal or interest were ever made on any of said debentures.

(s) Soon after the organization of said corporation, The Alaska Junk Company and Morris Schnitzer entered into a contract of guaranty whereby it was agreed that in the event a loss should be sustained by The Alaska Junk Company as a result of its extending credit to said corporation, Morris Schnitzer would pay to The Alaska Junk Company so much of any such loss as should exceed  $\frac{2}{3}$  of the total combined losses of himself and The Alaska Junk Company sustained on account of the extension of credit to said corporation by himself and The Alaska Junk Company, and a corresponding guaranty was made by The Alaska Junk Company to Morris Schnitzer to the extent of  $\frac{1}{3}$  of the total combine losses of said parties sustained through the extension of credit to said corporation.

(t) The idea for the establishment of said corporation was conceived by Morris Schnitzer and from its inception to July 17, 1943, he acted as its president and manager. On said date he was inducted into the armed service of the United States and this left the corporation without a directing head sufficiently informed and capable of carrying out the purposes of the corporation. Extended and repeated efforts were made to secure a suitable manager to take his place. None could be found. None of the remaining stockholders of said corporation or partners of The Alaska Junk Company were able to properly manage the plant. Its operation bogged down. There was a \$678,843.70 mort-



gage against its real estate. It owed \$149,650.00 for which its inventories were security, and in addition to the sums it owed, The Alaska Junk Company and Morris Schnitzer, it owed \$190,684.06 on open accounts. It lost money, became unable to pay its debts, and it became apparent that it would be impossible for it to carry on and operate profitably. Thereupon many industrialists of large financial ability were solicited in repeated efforts to find some person or organization that would take over the interests of The Alaska Junk Company and Morris Schnitzer in said corporation under such terms as would save them from loss, or at least, under terms that would result in as little loss to them as possible. Including those solicited were Kenneth B. Hall and A. M. Mears, then of the Hesse-Ersted Iron Works. After extended negotiations, an agreement was made by and between said Hall, Mears, The Alaska Junk Company, and Morris Schnitzer, by his attorney-in-fact Sam Schnitzer, whereby said Hall and Mears agreed to purchase the outstanding stock of said corporation at a nominal sum and thereafter to cause said corporation to execute and deliver a promissory note to the petitioner, Rose Schnitzer, Harry J. Wolf, Jennie Wolf, and Morris Schnitzer in the sum of \$249,000.00 to be secured by a second mortgage upon its properties in payment of all said debentures, and to execute and deliver a promissory note to said persons in the sum of \$151,000.00 secured by a third mortgage upon said properties in compromise and full payment of the balance due on



said open account and in complete satisfaction of a debt of \$26,493.77 then due and owing from said corporation to Morris Schnitzer. The Alaska Junk Company entered into said agreement for the reason that it gave The Alaska Junk Company the best opportunity it could find to realize the greatest possible amount on the obligations owed to it by said corporation.

(u) As evidence of the correct balance due The Alaska Junk Company on its said open account a demand promissory note in the amount of said balance was executed and delivered by said corporation to The Alaska Junk Company, and as evidence of the correct amount of said debt owed by said corporation to Morris Schnitzer a demand promissory note in the amount of said debt was executed and delivered by said corporation to Sam Schnitzer, the attorney-in-fact for Morris Schnitzer.

(v) On November 26, 1943, subsequent to the execution and delivery of the demand notes mentioned in paragraph V (u), all of the issued stock of said corporation was sold to said Hall and Mears and transferred to them or their order pursuant to the agreement mentioned in paragraph V (t); and thereafter said corporation executed and delivered promissory notes and a second and a third mortgage, and the same were accepted by The Alaska Junk Company and Morris Schnitzer, by his said attorney-in-fact, all in accordance with said agreement.

(w) Upon the receipt of said promissory note and second mortgage for the amount of \$249,000.00 all of the said debentures were returned to the said corporation as fully paid and satisfied, and The Alaska Junk Company credited its said open account with \$142,200.33, which was its pro-rata share of the said promissory note and third mortgage for \$151,000.00, and pursuant to said guaranty agreement charged Morris Schnitzer with \$83,581.20 and credited said open account with an equal amount, thereby reducing the balance of said open account to \$202,350.60, which balance became worthless within the calendar year 1943, because under the terms of the settlement with said corporation embodied in the agreement mentioned in paragraph V (t) no further amount could be realized on said unpaid balance from the corporation, and the said sum of \$83,581.20 was the entire amount for which Morris Schnitzer was liable under the said guaranty. On December 31, 1943, The Alaska Junk Company charged off the said balance as a bad debt, and nothing has since been received thereon.

(x) On account of the matters and things hereinabove stated The Alaska Junk Company sustained a bad debt or business loss in the calendar year 1943 in the sum of \$202,350.60.

(y) The Commissioner arbitrarily considered that the said unpaid and worthless balance of \$202,350.60 represented a contribution by The Alaska Junk Company to the capital of said corporation. There was no intention at any time by

the petitioner, or any of the other partners, that the said amount, or any portion thereof, should be a capital contribution to said corporation, but on the contrary it was the intention of The Alaska Junk Company that it was extending credit and that the full balance shown by its said open account would be repaid to it by said corporation.

Wherefore, the petitioner prays that this Court may hear this proceeding and determine that the petitioner has paid his tax in full for the calendar years in question and that there is no deficiency in income tax and/or victory tax due from the petitioner for the said years, and prays for such further relief as may be necessary and proper in the premises.

/s/ ROBT. T. JACOB,  
Counsel for Petitioner.

State of Oregon,  
County of Multnomah—ss.

Sam Schnitzer, being first duly sworn, says that he is the petitioner above named, that he has had the said petition read to him, and is familiar with the statements contained therein, and that the statements contained therein are true.

/s/ SAM SCHNITZER.

Subscribed and sworn to before me this 24th day of May, 1947.

[Seal]      /s/ J. F. JOHNSON,  
Notary Public for Oregon.

My Commission Expires March 28, 1951.

## Exhibit A

Treasury Department  
Internal Revenue Service  
Seattle 1, Washington

March 3, 1947

Office of Internal Revenue, Agent in Charge, Seattle Division, 305A Third Avenue Building

IT:90D:DLA

Mr. S. Schnitzer  
1011 S. W. Vista Avenue  
Portland 4, Oregon

Dear Mr. Schnitzer:

You are advised that the determination of your income tax liability for the taxable year ended December 31, 1943 discloses a deficiency of \$151,044.45 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days (not counting Saturday, Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with the Tax Court of the United States, at its principal address, Washington 25, D. C., for a redetermination of the deficiency or deficiencies.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, Seattle 1, Washington for the attention of IT:90D:DLA. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency or deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

JOSEPH D. NUNAN, JR.,

Commissioner,

By /s/ S. R. STOCKTON,

Internal Revenue Agent  
in Charge.

DLA:mts

Enclosures

Statement

Form of waiver



## Statement

IT:90D:DLA

Mr. S. Schnitzer  
1011 S. W. Vista Avenue  
Portland 4, Oregon

Tax liability for the taxable year ended December 31, 1943.

	Deficiency
Income tax .....	\$151,044.45

In making this determination of your income tax liability, careful consideration has been given to the report of examination dated June 3, 1946, to your protest dated October 23, 1946, and to the statements made at the conference held on January 22, 1947.

A copy of the letter and statement has been mailed to your representative, Robert T. Jacob, in accordance with the authority contained in the power of attorney executed by you.

## Taxable Year Ended December 31, 1942

Adjustments to Net Income	
Net income as disclosed by return.....	\$ 58,995.58
Unallowable deductions and additional income:	
(a) Income from partnership .....	54,030.86
Total .....	\$113,026.44
Nontaxable income and additional deductions:	
(b) Contributions .....	723.04
Net income adjusted .....	\$112,303.40

## Explanation of Adjustments

(a) It has been determined from an examination of the 1942 return filed by the partnership, Alaska Junk Co., that your distributive share of the income of that partnership was \$118,061.72. Reported on the return, \$64,030.86. Additional income from partnership, \$54,030.86.

(b) It has been determined that your share of contributions made by the partnership, Alaska Junk Co., is \$1,446.08. Deducted on the return, \$723.04. Additional deduction allowed, \$723.04.

Computation of Tax

Net income, adjusted .....	\$112,303.40
Less: Personal exemption .....	1,200.00
Surtax net income .....	\$111,103.40
Less: Earned income credit .....	1,400.00
Balance subject to normal tax .....	\$109,703.40
Normal tax at 6 per cent on \$109,703.40 ..	\$ 6,582.20
Surtax on \$111,103.40 .....	67,911.69
Total tax .....	\$ 74,493.89

Taxable Year Ended December 31, 1943

Adjustments to Net Income

	Income Tax Net Income	Victory Tax Net Income
Net income as disclosed by return .....	\$ 61,827.03	\$ 66,670.04
Unallowable deductions and additional income:		
(a) Income from partnership .....	157,689.23	157,689.23
Total .....	\$219,516.26	\$224,359.27
Nontaxable income and additional deductions:		
(b) Contributions .....	981.08	
Net income adjusted .....	\$218,535.18	\$224,359.27

Explanation of Adjustments

(a) It has been determined from an examination of the 1943 return filed by the partnership, Alaska Junk Co., that your distributive share of the income of that partnership was \$224,203.15. Reported on the return \$66,513.92. Additional income from partnership, \$157,689.23.

(b) It has been determined that your share of contributions made by the partnership, Alaska Junk Co., is \$1,962.16. Deducted on the return, \$981.08. Additional deduction allowed, \$981.08.

## Computation of Income and Victory Tax

Income tax net income, adjusted .....	\$218,535.18
Less: Personal exemption .....	1,200.00
Surtax net income .....	\$217,335.18
Less: Earned income credit .....	1,400.00
Balance subject to normal tax .....	\$215,935.18
Normal tax at 6% on \$215,935.18.....	\$ 12,956.11
Surtax on \$217,335.18 .....	153,354.85
Total income tax .....	166,310.96
Victory tax net income adjusted .....	\$224,359.27
Less: Specific exemption .....	624.00
Income subject to victory tax .....	\$223,735.27
Victory tax before credit, 5% of \$223,735.27 .....	11,186.76
Less: Victory tax credit .....	500.00
Net victory tax .....	10,686.76
Net income tax and victory tax .....	\$176,997.72
Income tax for 1942 .....	\$ 74,493.89
Amount of net income tax and victory tax .....	\$176,997.72
Forgiveness feature:	
(a) Amount of Income tax for 1942....	\$ 74,493.89
(b) Amount forgiven ( $\frac{3}{4}$ of (a) ) ....	55,870.42
(c) Amount forgiven .....	18,623.47
Total income and victory tax liability .....	\$195,621.19
Income and victory tax liability disclosed by return Account No. 353531 .....	44,576.74
Deficiency of income tax .....	\$151,044.45

Received and filed T.C.U.S. May 26, 1947.

[Title of Tax Court and Cause.]

### ANSWER

Comes Now the Commissioner of Internal Revenue, by his attorney, Charles Oliphant, Acting Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed herein, admits, denies and alleges as follows:

I. Admits the allegations contained in paragraph I of the petition.

II. Admits the allegations contained in paragraph II of the petition.

III. Admits that the taxes in controversy are, in part, income taxes for the calendar years 1942 and 1943, and that the amount of tax so in controversy is, to wit: \$151,044.45. Denies the remaining allegations contained in paragraph III of the petition. Alleges that said amount of, to wit: \$151,044.45, consists, in part, of victory tax for the year 1943, and that by reason of the forgiveness feature of section 6 of the Current Tax Payment Act of 1943, he, the Commissioner, had determined a deficiency in income and victory tax only for the year 1943.

IV(a) to (d), inclusive. Denies that he erred in his determination of the deficiency as shown by the notice of deficiency from which petitioner's appeal is taken. Specifically denies that he erred in the manner and form as alleged in paragraph IV(a) to (d), inclusive, of the petition.

V(a). Denies the allegations contained in paragraph V(a) of the petition.

(b) Admits his refusal to recognize that Rose Schnitzer and Jennie Wolf were partners in said business in the calendar years 1942 and 1943. Denies the remaining allegations contained in paragraph V(b) of the petition.

(c) Admits that petitioner and Rose Schnitzer were intermarried, and now are, and ever since have been, husband and wife. For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth or falsity thereof, denies the remaining allegations contained in paragraph V(c) of the petition.

(d) to (h), inclusive. For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth or falsity thereof, denies the allegations contained in paragraph V(d) to (h), inclusive, of the petition.

(i) to (m), inclusive. Denies the allegations contained in paragraph V(i) to (m), inclusive, of the petition.

(n) For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth or falsity thereof, denies the allegations contained in paragraph V(n) of the petition.

(o) For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth or falsity thereof, denies the allegations contained in paragraph V(o) of the petition. Specifically denies that Rose Schnitzer and Jennie Wolf



were partners in the business known and carried on under the name of the Alaska Junk Company.

(p) to (w), inclusive. For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth or falsity thereof, denies the allegations contained in paragraph V(p) to (w), inclusive, of the petition.

(x) Denies the allegations contained in paragraph V(x) of the petition.

(y) Admits that he, the Commissioner, considered the balance of \$202,350.60 as a capital investment. Denies the remaining allegations contained in paragraph V(y) of the petition.

VI. Denies generally and specifically each and every material allegation contained in the petition, not hereinbefore specifically admitted, qualified, or denied.

Wherefore, it is prayed that the petitioner's appeal be denied and that the Commissioner's determination of deficiency be approved.

/s/ CHARLES OLIPHANT, JHP,

Acting Chief Counsel, Bureau  
of Internal Revenue.

Of Counsel:

B. H. NEBLETT,

Division Counsel,

JOHN H. PIGG,

R. G. HARLESS,

Special Attorneys,

Bureau of Internal Revenue.

Received and filed T.C.U.S., August 7, 1947.



[Title of Tax Court and Cause.]

MOTION AND ORDER TO  
AMEND PETITION

Comes now the petitioner in the above entitled cause by Robt. T. Jacob, his counsel of record, and moves the Court for an order permitting him to amend his petition by adding to paragraph V of said petition immediately after sub-paragraph (m) of paragraph V a sub-paragraph to be designated (m.1) in form and substance as follows:

(m.1) During the year 1944 the petitioner instituted proceedings in the Tax Court of the United States against the Commissioner of Internal Revenue by filing in said court a petition docket number 6264, appealing from a purported deficiency in income taxes for the calendar year 1941, in which petition the petitioner, among other things, alleged:

“(a) Petitioner is a member of the partnership of Alaska Junk Company, which said partnership is composed of four individuals, H. J. Wolf, Mrs. J. Wolf, S. Schnitzer and Mrs. R. Schnitzer, each owning a one-fourth interest therein.”

The Commissioner of Internal Revenue filed his answer to said petition in said court and in his answer admitted the above quoted allegation. Docket numbers 6262, 6263 and 6265 were similar proceedings instituted respectively by Harry J. Wolf, Jennie Wolf and Rose Schnitzer, and in the petitions in each of these dockets there was an allegation similar to the one above quoted, and in the answer

to each said petition the Commissioner admitted said allegation. Thereafter the said proceeding docket number 6264, and the related dockets 6262, 6263 and 6265 were consolidated for trial and tried by the said Tax Court of the United States, and on or about the 23rd day of December, 1946, the said Tax Court of the United States made and entered findings of fact and its opinion, in which findings of fact the said court found:

“The petitioners are husbands and wives and members of a co-partnership, doing business under the firm name and style of Alaska Junk Company at Portland, Oregon. Each petitioner had a one-fourth interest in the firm. They filed individual income tax returns with the collector of internal revenue for the district of Oregon.

“The partnership, Alaska Junk Company, was originally organized by petitioners, H. J. Wolf and S. Schnitzer, in 1911. Its business was the buying and selling of all sorts of salvage metals and materials. The original partnership continued until 1925 or 1926 when the wives of the partners, petitioners Jennie Wolf and Rose Schnitzer, were taken into the firm. That partnership is still in existence except that petitioner Jennie Wolf, the wife of H. J. Wolf, died in April 1945.”

On or about the 24th day of September, 1946, the said Court entered its decisions in each of the said causes and each of the said decisions, less formal parts, date, seal and signature, is as follows:

“Pursuant to the determination of the Court, as

set forth in its Memorandum Findings of Fact and Opinion, entered Sept. 23, 1946, it is

Ordered and Decided: That there is no deficiency in income tax for the calendar year 1941."

That the findings and decision in docket 6264 was a final adjudication in favor of the petitioner and against the Commissioner of Internal Revenue. Petitioner is named in said docket 6264 as S. Schnitzer. The interest of the petitioner, Rose Schnitzer, Harry J. Wolf and Jennie Wolf in said Alaska Junk Company were exactly the same in the calendar years 1942 and 1943 as in the year 1941, and the fact that each of the said persons has said interests in said partnership during said years has become *res judicata* and the Respondent ought to be and is estopped to deny the same.

/s/ ROBT T. JACOB,

Counsel for Petitioner.

Granted June 10, 1948. Luther A. Johnson, Judge.

Filed T.C.U.S. June 10, 1948.

Copy served N.A.L.

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[Title of Tax Court and Cause.]

## ANSWER TO AMENDMENT TO PETITION

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for answer to the amendment to

petition filed by the above-named petitioner admits and denies as follows:

V-(m.1) Admits the allegations contained in subparagraph (m.1) of paragraph V of the petition except that it is denied that the findings and decision in Docket 6264 was a final adjudication in favor of the petitioner and against the Commissioner of Internal Revenue; that the interest of the petitioner, Rose Schnitzer, Harry J. Wolf and Jennie Wolf in said Alaska Junk Company were exactly the same in the calendar years 1942 and 1943 as in the year 1941, and the fact that each of the said persons has said interests in said partnership during said years has become *res judicata* and the respondent ought to be and is estopped to deny the same.

/s/ CHARLES OLIPHANT,  
Chief Counsel, Bureau of  
Internal Revenue.

Of Counsel:

B. H. NEBLETT,  
Division Counsel,

JOHN H. PIGG,  
LEONARD A. MARCUSSEN,

Special Attorneys,  
Bureau of Internal Revenue.

Received and filed T.C.U.S. July 28, 1948.

Served July 29, 1948.

13 T. C. No. 8

The Tax Court of the United States

Docket Nos. 14208, 14209, 14278, 14279, 14280, 14372

SAM SCHNITZER,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.ESTATE OF HARRY J. WOLF, Deceased, by  
MONTE L. WOLF, the Executor of said  
Estate,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

MONTE L. WOLF,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.



BLOSSOM M. GOLDSTEIN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

CHARLOTTE C. COHON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

ESTATE OF JENNIE WOLF, Deceased, by  
MONTE L. WOLF, Administrator de bonis  
non with the will annexed of said Estate,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Promulgated July 14, 1949.

### FINDINGS OF FACT AND OPINION

Two individuals, engaged for many years in the junk business, signed a partnership agreement in 1928, giving to the wife of each a one-fourth interest. When the husbands began the junk business in a humble way, the wives' dowries in part sup-

plied capital, and the wives also gave assistance by services. As the business expanded into a large and profitable enterprise, the wives were constantly consulted about policy; the husbands deferred to their judgment in business matters, and they participated fully and often decisively in important decisions. For 1941 the four spouses successfully contested tax deficiencies which the Commissioner had determined against them by disallowing as excessive a part of the salaries paid by the partnership to family members, and in its report this Court made a finding that the four were conducting business as partners, as alleged by them and admitted by the Commissioner. For 1942 and 1943 the Commissioner determined that the wives were not recognizable as partners for tax purposes.

1. The status of the wives as partners recognizable for tax purposes, held, not *res judicata* by virtue of the decision in the prior proceeding, and as the question was not there put in issue, the Commissioner is not collaterally estopped to raise it here. *Commissioner v. Sunnen*, 333 U. S. 591.

2. On the evidence, held, that the wives are recognizable for tax purposes as members of the partnership.

The partnership and the son of a partner in and after 1941 made numerous advances on open account to a corporation organized with an authorized capital of a quarter of a million dollars to erect and operate a steel mill. The corporation issued its shares to the son, the partners and their wives, and

in March 1943, when advances aggregated about three-quarters of a million dollars, entries were made on the books of the partnership and of the son's business crediting \$187,800 to payment for the shares issued, which were of that par value; about a quarter of a million dollars to payment for corporate bonds issued in that amount, and the remainder was carried on open accounts receivable by the partnership and son and on corresponding open accounts payable by the corporation. Under a contract with RFC the corporation was forbidden to make any payments (except salary) to the stockholders until a \$700,000 RFC loan should be paid off by it, and the stockholders agreed among themselves that the son, who held one-third of the shares, was to bear one-third of any total losses from the venture, and the partnership, two-thirds. The corporation was unsuccessful and in November 1943 the stockholders sold their shares at one cent each and about \$300,000 of the open accounts was written off as worthless. By contribution from the son the partnership's share of this loss was reduced to about \$200,000.

On the evidence, held, that the advances constituted contributions to capital, and the partnership's loss is hence not deductible as a bad debt.

Robt. T. Jacob, Esq., and Randall S. Jones, Esq., for the petitioners.

Leonard A. Marcussen, Esq., for the respondent.

The Commissioner determined a 1943 income tax deficiency of \$151,044.45 against Sam Schnitzer; of

\$151,049.05 against Harry J. Wolf, now deceased; and of \$42,273.99 against the estate of Jennie Wolf, deceased. He determined further that Monte L. Wolf, Blossom M. Goldstein and Charlotte C. Cohon are liable for the deficiency of Jennie Wolf's estate as transferees of all the estate's assets. The deficiencies determined against Sam Schnitzer and Harry J. Wolf, deceased, resulted from the inclusion in each one's income of one-fourth of the profits of a partnership, which fourth had been reported by their respective wives as partners. The deficiency against the estate of Jennie Wolf resulted from an alternative determination that she was recognizable as a partner. In all three determinations the distributable shares of partnership profits were increased by disallowance of a bad debt deduction claimed by the partnership on account of the worthlessness of advances made by it to a corporation in which Sam Schnitzer, Harry J. Wolf and their wives were stockholders. Petitioners contend that the wives were bona fide members of the partnership and recognizable as such for tax purposes; that the partnership's advances to the corporation were loans, not contributions to capital, as respondent contends, and the part of them which became worthless and was written off in 1943 is deductible as a bad debt.

### Findings of Fact

Sam Schnitzer, petitioner in Docket No. 14208, and Harry J. Wolf, deceased, residents of Portland,



Oregon, in 1942 and 1943, prepared their income tax returns for those years on the cash basis and filed them with the collector of internal revenue for the district of Oregon. Harry J. Wolf died on February 6, 1948, and his son, Monte L. Wolf, is executor of his estate, petitioner in Docket No. 14209. Monte L. Wolf is also administrator de bonis non with the will annexed of the estate of Jennie Wolf, deceased, petitioner in Docket No. 14372. Jennie Wolf, wife of Harry J. Wolf, died on April 8, 1945, a resident of Portland, and the owner of property in excess of the deficiencies in tax asserted against her. She filed her income tax returns, prepared on the cash basis, for 1942 and 1943 with the collector of internal revenue for the district of Oregon. Monte L. Wolf, Blossom M. Goldstein and Charlotte C. Cohon, petitioners in Docket Nos. 14278, 14279 and 14280, also residents of Portland, are children of Harry J. and Jennie Wolf, and received, as distributees of the residue of Jennie Wolf's estate, assets of a fair market value of \$22,923.09, \$23,855.57 and \$24,112.08, respectively. The distribution of these assets left the estate without means to pay taxes, and these petitioners became thereby liable as transferees for any deficiency in tax of the transferor estate to the extent of the value of property received by each.

During the years 1942 and 1943 Sam Schnitzer and Harry J. Wolf were active in the operation of the Alaska Junk Co. (hereafter called Alaska Junk), a partnership engaged in the business of



buying, selling and generally dealing in junk, pipe, tools, machinery, hardware, scrap and other metal products in Portland. Its books were kept on an accrual basis, and partnership returns, prepared on that basis, were filed for it in 1942 and 1943 with the collector of internal revenue for the district of Oregon. On these returns Sam Schnitzer and his wife, Rose Schnitzer, Harry J. Wolf and his wife, Jennie Wolf, were listed as the partners, and a share of profits was reported as distributable to each.

Wolf and his wife were married at Portland in 1906. Both were born abroad, but the wife had been educated in this country and spoke fluent English. Wolf did not. Her father was engaged in the junk business and employed Wolf as an assistant, but Wolf was unhappy in his work because his handicap exposed him to ridicule. He remained with his father-in-law long enough to know the various metals, and as his wife was familiar with the junk business, they decided to operate independently. She had brought a dowry of about \$1,000, and with this Wolf purchased a horse and wagon, and began to collect scrap metal in rural areas on trips that sometimes lasted two weeks or more. This scrap was stored in the basement of their home, and his wife took customers' calls, kept records, and performed those duties of the business which required writing. Schnitzer and his wife were also born abroad. She brought the customary dowry, and Schnitzer began to buy and sell scrap metal also, developing a busi-

ness in a petty way with his wife's aid. About 1911 Wolf and Schnitzer began working together in the junk business, Wolf contributing his horse and wagon and some machinery and Schnitzer providing about \$1,000 capital. In February, 1912, they and S. Horwitz organized a corporation to engage in the junk business, and one share of \$1,000 par value was issued to each of the three. Because of differences with Horwitz the corporation was dissolved the following April. Thereafter Wolf and Schnitzer jointly operated a junk business without any formal agreement, and developed it into a large and profitable enterprise. The two families were on intimate terms during the ensuing years, and there were daily discussions of business problems and policies by the four at one or the other's home or at the business office. In these conferences the wives took an active part, especially Jennie Wolf, whose business acumen was respected by both husbands.

On January 3, 1928, the four spouses entered into a written agreement which recited that the two husbands "in consideration of love and affection \* \* \* desire to admit" the two wives "as co-partners" in the business of buying and selling machinery, iron and iron products, which "S. Schnitzer and H. J. Wolf have heretofore carried on \* \* \* under the names of Alaska Junk Company and Schnitzer-Wolf Machinery Company." It was then agreed that the two husbands "assign, sell and transfer" to their respective wives a one-fourth interest in the business; that the husbands carry on the

business in the same manner as before; that active management and control be vested in them and that they have the exclusive right to enter into contracts, to obligate the partnership on notes, bills and orders; to sign all checks, and to determine all questions of management and policy. The interest of each partner was fixed as one-fourth; each was to be allowed to draw weekly wages for services, and after deduction of these wages and other business expenses, the resulting net profits were to be divided equally by the four and losses were to be so borne. The four immediately signed and publicly recorded an Assumed Name Certificate to do business as the Alaska Junk Company. Books were opened, and a capital account was set up for the four.

Thereafter withdrawals were made by each husband and charged to a drawing account in his name. The husband's withdrawals included money used for household expenses, and the partnership paid directly some domestic bills, the amount being charged to the debtor husband's account. Later a drawing account was set up for each wife, but the wives' drawing accounts were charged only with their income taxes, which the partnership paid, and the wives never made any direct withdrawals. Undrawn profits were left in the business, and at the end of the year the drawing accounts of spouses were consolidated and if one family had drawn more than the other, the excess was charged to the excess drawing husband's account. Undrawn profits were then credited to capital account. As the two

families lived frugally, a substantial amount of profits was accumulated over the years and used in the business. Each husband was paid a salary of \$10,000 a year for his services in 1938 and thereafter. Constant conferences between the four spouses were continued. The wives kept in close touch with all phases of the business, and no important decision was reached without their participation. Proposals for several new enterprises were dropped because of their opposition, and other ventures were undertaken only after their approval. They rendered vital services to the partnership in 1942, 1943 and preceding years, and their dowries constituted a material capital factor in the original launching of a junk business by each husband.

Prior to 1928 Wolf and wife and Schnitzer and wife did not file separate income tax returns. Since 1928 profits of the business have been reported on partnership returns which indicated one-fourth as the share distributable to each of the four, and each has reported the share on a separate return. A copy of the partnership agreement was furnished an examining revenue agent prior to 1931, and the Commissioner accepted the returns as correctly reporting the partnership's members and interests until 1942. In 1938 and subsequent years the distributable shares have been computed to reflect \$10,000 more for each husband.

Accepting the partnership return, the Commissioner increased the distributable profits reported for 1941 by disallowing as excessive compensation



a bonus of \$10,000 each paid to a son and son-in-law of Schnitzer and to a son and son-in-law of Wolf, who were employed in the business in that year. Schnitzer and wife and Wolf and wife each filed a petition with this Court, Docket Nos. 6262-5, contesting the determined increase in distributable income and the tax thereon, which resulted from the change, and assigning as error the Commissioner's disallowance of "certain salaries paid by the Alaska Junk Company." Each petitioner alleged that he was "a member of the partnership of Alaska Junk Company, which said partnership is composed of four individuals, H. J. Wolf, Mrs. J. Wolf, S. Schnitzer and Mrs. R. Schnitzer; each owning a one-fourth interest therein." Respondent admitted the allegation in his answers, and this Court found it as a fact. It also found that the partnership was originally organized in 1911 by Wolf and Schnitzer. After stating that the only issue was the "purely fact question" of "the reasonableness of salaries paid to the four sons and sons-in-law," the Court decided that the amounts paid were reasonable and reversed the Commissioner's determinations by decision entered September 24, 1946.

As Alaska Junk expanded its activities and grew in financial strength, it occasionally made loans or advances to customers in the expectation of maintaining or increasing its trade. These advances were made some times when the customer was indebted to it for goods and were charged to his open account. The books indicate such advances aggregat-



ing \$1,600 to M. Turn; \$4,479.63 to Munce & Pedrante; \$1,510 to R. Pedrante; \$2,750 to Emil Nyberg; \$4,500 to the Marshfield Bargain House; \$8,000 to the Medford Bargain House, and \$1,971.08 to various others. All of these customers bought scrap and sold it to Alaska Junk or hauled scrap for Alaska Junk, and most of the advances were repaid by cash or by credit for scrap supplied. Some were not repaid.

Alaska Junk also made very large advances to enterprises in which members of the Wolf and Schnitzer families were interested. Schnitzer's son, Morris, individually operated a scrap business under the assumed name of Schnitzer Steel Products Co. Between July, 1936, and March, 1948, Alaska Junk made to him cash advances aggregating \$119,020.99, of which \$17,517.37 was repaid in cash and the rest in scrap. In 1939 Wolf, Schnitzer and their wives organized the Central Supply Co. as a wholesale dealer in plumbing and electric goods. The organizers, in payment for its capital stock, placed \$50,000 to its credit in an account with Alaska Junk, and Alaska Junk thereafter made to it aggregate cash advances of \$15,500, and also sold it goods. Charges to the account have been paid. In 1939 Wolf, Schnitzer and their wives and Morris Schnitzer incorporated Industrial Air Products Co. for the manufacture of oxygen and acetylene. Alaska Junk was charged with the amount of the stock subscription; thereafter made cash advances aggregating \$94,427.03, and has sold merchandise to

the company. Repayment has been made. In 1940 Wolf, Schnitzer and their wives and one Shea organized Plumbing and Heating Sales Co. Alaska Junk again advanced the money for its capital; made sales to it and purchases from it. In 1941 Alaska Junk and Dulien Steel Products Co. formed the Carlton Coast Railroad Liquidators as a joint venture to acquire and dismantle a logging camp and railroad and to sell the salvaged materials. Alaska Junk advanced \$27,525 for the venture; acquired a 50 per cent participation, and has received from it \$134,649.94. The partnership kept open accounts with all the persons and firms to whom the above mentioned advances were made, charging to such accounts all cash advanced and merchandise furnished, and crediting them with payments in cash or in goods bought by it.

On June 4, 1941, Morris Schnitzer, son of Sam Schnitzer, organized the Oregon Electric Steel Rolling Mills (hereafter called Oregon Steel) as an Oregon corporation with an authorized capital of \$250,000, represented by 2,500 shares of stock of a par value of \$100 each. Of the authorized shares subscription was made for 1,878 as follows:

Morris Schnitzer	1,250	per value	\$125,100
Sam Schnitzer	312½	" "	31,250
Harry J. Wolf	312½	" "	31,250
Bernard Levin	1	" "	100
Louis Schnitzer	1	" "	100

On June 12, 1941, one share was issued to each of the five subscribers; on August 4, one share was issued to L. N. Rosenbaum, and on February 10, 1942, 1,251 shares were issued to Morris Schnitzer;  $312\frac{1}{2}$  to Sam Schnitzer and  $312\frac{1}{2}$  to Harry J. Wolf. On February 10, 1942, Sam Schnitzer and Wolf surrendered their  $312\frac{1}{2}$  share certificates and four new certificates for  $156\frac{1}{4}$  shares each were issued to each of them and their wives. There were also changes in the holders of one share.

Oregon Steel was organized to erect and operate a rolling mill for the manufacture of steel products. Its stockholders planned to melt down and use scrap metal, which in 1941 was being sold in Portland at \$1.50 to \$2 a ton less than in Seattle, and on the basis of engineers' production estimates expected the earnings eventually to reach \$50,000 or more a month. Morris Schnitzer, with whom the idea originated, was made president and general manager. He had been engaged for some years in the purchase and sale of new and used iron, steel, tools and machinery in Portland under the trade name of Schnitzer Steel Products Co.; had had considerable experience in salvage enterprises in various parts of the country, and had studied engineering and business administration at the University of Washington. He was active in seeking capital for Oregon Steel, in getting engineering advice and trade information, and in procuring materials and the necessary priorities. He consulted various steel men and jobbers, arranging outlets for prospective products,

jobbers, arranging outlets for prospective products, and made numerous business trips to New York and Washington. He experienced great difficulties in getting the enterprise started, and actual construction of the mill did not begin until November, 1942. Sam Schnitzer, the vice president, and Harry J. Wolf, the secretary, also rendered services. The corporation's board of directors was composed of Morris, Sam and Rose Schnitzer and Harry J. and Jennie Wolf. None of them had had any experience in steel production.

From October 1941 Alaska Junk made numerous advances of cash to Oregon Steel; supplied it with goods of various kinds at cost and paid bills for it. The amounts of cash advance, the bills paid and value of the goods furnished were charged to its open account with Alaska Junk. As Alaska Junk had less than \$10,000 cash normally on hand, it often made bank loans to provide cash advances. Morris Schnitzer likewise advanced cash, paid bills and supplied goods, and these amounts, together with the expenses of his business trips, were charged to the corporations account with Schnitzer Steel Products Co. Nearly all of the advances were for plant and equipment but after operations began \$9,460 in scrap was furnished by Alaska Junk. All of the foregoing charges were reflected by corresponding credits to the accounts of Alaska Junk and Schnitzer Steel Products Co. on the corporation's books. On November 30, 1942, the corporation's account with Alaska Junk showed a debit balance of \$299,069.70 and its account with Sch-



nitzer Steel Products Co., a debit balance of \$138,984.11. On an office memorandum Sam Schnitzer referred to those advances as "contributed capital."

During 1941 Morris Schnitzer made numerous attempts to procure outside capital. In June he besought New York investment banking houses to make a public offering of Oregon Steel's stock, but they declined on the grounds that no proper engineering reports had been submitted and the organizers lacked adequate experience. The Commercial Credit Corporation refused to make a loan because they deemed the \$250,000 authorized capital too small. For the same reasons the Bank of America refused a loan in November 1941. The Bank of Portland refused a loan in April 1942, despite oral assurances by the corporation's officers that \$1,000-000 would be invested in the plant and more would be available for working capital. In October 1941 the corporation filed application with the Reconstruction Finance Corporation for a loan of \$600,000 and employed the engineering firm of MacDonald Bros., Inc., to make a survey and report on the necessary investment and probable operating costs. On this application Morris Schnitzer, signing as president, stated that the corporation proposed to expend \$550,000 of the proceeds on buildings and equipment and \$50,000 on raw materials, brick, manganeses, scrap, etc. He estimated that the plant would cost \$890,000; stated that capital was then \$187,700 but added:

We expect to increase the capital of this corporation shortly. Additional stock will be taken by S.



Schnitzer and J. Wolf to equal that of M. Schnitzer.

On the MacDonald report, filed with the RFC on November 10, 1941, cost of the mill and equipment was put at \$987,035, exclusive of engineering, legal, traveling and organization expenses. Organization expenses were given as \$65,000.

The RFC was not satisfied with the MacDonald report, and a second was submitted from another engineer, who estimated that the mill would cost \$1,050,000. On April 2, 1942, the executive committee of the RFC approved the loan, subject to listed conditions. After several changes had been made in the conditions, Sam Schnitzer and Wolf, as partners of Alaska Junk, wrote RFC on December 1, 1942, that cost of the mill might exceed \$1,200,000 and that Alaska Junk would furnish any necessary money in excess thereof to complete the project if RFC would lend an additional \$100,000. On December 4, 1942, RFC approved a loan of \$700,000, having received assurance that there had been no change in the borrower's financial condition and business prospects. Oregon Steel gave to the Federal Reserve Bank of San Francisco its 4 per cent promissory note for that amount, dated December 15, 1942, payable within five years by monthly installments of \$6,500 from May 1, 1943, and by an additional annual payment sufficient to make all payments equal to 50 per cent of the corporation's net earnings for the preceding year. The note was secured by a duly recorded mortgage on the corporation's real estate and the plant to be con-

structed and equipped and on its personal property with the exception of cash, receivables, raw materials and inventories. Effective supervisory powers were given to RFC to enforce current compliance with the terms.

By separate agreement Morris, Sam and Rose Schnitzer and Harry J. and Jennie Wolf individually guaranteed repayment of the note, and bound themselves to supply "additional working capital" in amounts deemed satisfactory by FRC as long as any part of the loan should remain unpaid. The corporation bound itself to limit officers' annual salaries for such period to a total of \$25,000, and to pay in cash no more than \$15,000. In an instrument of December 29, 1941, the corporation, Morris Schnitzer and Alaska Junk recited that Morris Schnitzer and Alaska Junk had already contributed \$138,984.11 and \$299,069.70, respectively, in the form of cash or property to the corporation; that:

Such contributions by stockholders have, as stated, been as a capital investment, and in no wise as outstanding accounts payable by Borrower, except to the extent that Borrower's debenture notes may be issued for a part of such contributions or capital investment.

And the stockholders agreed that they would receive in payment of "all such capital investments so made" only the common stock or debenture notes of the corporation and the corporation in turn covenanted to make payments in no other way. The corporation further agreed that as long as any part

of the RFC loan should remain unpaid, it would not issue to stockholders any preferred stock or evidence of indebtedness except debentures on a prescribed form "in return for advances made or to be made by them." The prescribed form forbade payment of principal or interest on the debentures until full repayment of the RFC loan. These conditions were observed, but RFC did allow reimbursement for about \$114,519 of subsequent advances for the purchase of mill equipment.

While the final terms of the RFC loan were being arranged, Wolf expressed dissatisfaction because Morris Schnitzer, holding two-thirds of the corporate stock, had not made a proportionate part of the advances. Costs of the enterprise had already exceeded anticipations, and Morris was financially unable to advance more. The stockholders entered into negotiations among themselves for a more satisfactory distribution of interests. They reached an agreement, and pursuant thereto the corporate directors authorized issuance of debenture bonds for \$250,000 on terms contemplated by the understanding with RFC. On January 12, 1943, it issued such bonds in an aggregate of \$249,000 to its stockholders in the following amounts:

Morris Schnitzer .....	\$75,000
Sam Schnitzer .....	44,000
Rose Schnitzer .....	43,000
Harry J. Wolf .....	44,000
Jennie Wolf .....	43,000

These bonds bore 8 per cent interest and were payable within ten years of issue, but no payment of interest or principal could be made while any balance remained due on the corporation's \$700,000 note to RFC.

As part of the settlement agreement Morris Schnitzer on March 11, 1943, surrendered 626 of his 1,251 shares of stock. One share was reissued to Monte L. Wolf and the remainder to Sam Schnitzer and wife and Harry J. Wolf and wife so that the corporation's 1,878 outstanding shares were thereafter held as follows:

	Shares
Morris Schnitzer .....	625
Sam Schnitzer .....	313½
Rose Schnitzer .....	312½
Harry J. Wolf .....	313½
Jennie Wolf .....	312½
Monte Wolf .....	1

By entries of March 31, 1943, the corporation charged the open account of Schnitzer Steel Products Co. (Morris Schnitzer) with \$75,000 for "debentures issued" and with \$62,500 "to offset bal. of stock subscriptions due against Acc. Pay.," leaving a credit balance of \$6,638.23 in the account. By entries of the same date it charged Alaska Junk's open account with \$174,000 "to record debentures issued" and with \$124,900 "to offset bal. of stock subscriptions due against Acc. Pay.," leaving a balance of \$315,095.41 in that account. By entries of



July 14, 1943, Alaska Junk credited the corporation's account by corresponding amounts, specifying that the shares and bonds had been issued to Sam and Rose Schnitzer and to Harry J. and Jennie Wolf in the amounts above set forth. No other shares were ever issued although in the beginning the organizers expected to issue more to associate promoters.

In connection with the bond issue and stock transfer Morris Schnitzer orally agreed with Sam and Rose Schnitzer and Harry J. and Jennie Wolf that he would bear one-third of any loss that might result from the total amounts advanced and to be advanced by all five to the corporation, over and above the advances credited to stock subscriptions. They in turn agreed to bear two-thirds of any such loss. Morris Schnitzer and Alaska Junk continued thereafter to make advances, as before, and these advances were credited to their open accounts with the corporation in the same way as before, and charged to the corporation's open accounts with them.

In asking for larger releases of the authorized loan, Morris Schnitzer on March 18, 1943, wrote RFC that costs were rising, and that the stockholders had "in this job over \$700,000 of our own money," but "never originally intended to put in over \* \* \* the \$500,000 we were supposed to put in as our share in the capital investment." In a prior letter of December 23, 1942, he had referred to "additional costs for the extensions and additions"



to the plant, suggested in the McKee report to increase production capacity, and requested approval of them.

Construction work on the mill began in November 1942, but building materials were hard to obtain; new machinery was scarce; priorities could not be procured for some requirements, and second-hand equipment and materials had to be used in part. Prices steadily increased. The mill was finally completed in June 1943 at a cost of \$1,400,000, and the melting of scrap into ingot started soon thereafter. About the same time Morris Schnitzer entered military service, and his brother, Manuel Schnitzer, who had been employed by the corporation since the preceding January, took charge. Manuel was not familiar with steel manufacture; two engineers, successively engaged as managers, proved unsatisfactory, and competent personnel and operators were difficult to find. Manuel made vigorous efforts, however, and rolling operations were begun late in August. But the machinery did not function properly; production was so far behind schedule that many large orders were cancelled by customers, principally the United States Government; creditors pressed for the payment of bills; there was a lack of ready cash, and a serious financial crisis developed. In June 1943 the corporation began to get some relatively small loans from banks, secured by its steel inventory and warehouse receipts for scrap. By November 26 these amounted to \$149,499.71.

The stockholders again tried unsuccessfully to

interest outsiders to take a participating interest, and approached the United States Steel Co., Bethlehem Steel Co., Republic Steel Co., Henry Kaiser and others. But in November 1943 they ceased operations, and on November 26 decided to withdraw from the enterprise entirely, and to sell all their shares to Kenneth E. Hall and A. M. Mears for one cent a share. Before so doing, they had the corporation give to Schnitzer Steel Products Co. its promissory note for \$26,829.28 and to Alaska Junk its promissory note for \$427,843.87. The amounts of these notes were equal to the respective credit balances shown on that date in the payees' open accounts with the corporation, but as later computed such balances were in fact \$26,493.77 and \$428,132.13, respectively. That of Alaska Junk reflected the following aggregate debits and credits:

#### Debits

Cash advanced .....	\$327,870.23
Bills paid .....	166,340.16
Goods furnished .....	347,321.62
<hr/>	
Total .....	\$841,552.01

#### Credits

Stock .....	\$124,900.00
Bonds .....	174,000.00
Repayments .....	114,519.88
<hr/>	
Total .....	\$413,419.88

Immediately after the sale the purchasers elected new officers and directors, Mears becoming president. Pursuant to a resolution of the new directors and with consent of RFC, the corporation gave to Morris, Sam and Rose Schnitzer and Harry J. and Jennie Wolf its 6 per cent note for \$249,000 payable in annual installments of \$24,900 beginning June 1, 1954, and secured by a second mortgage on the corporation's property. It also gave to them its 6 per cent note for \$151,000 payable in annual installments of \$15,100 beginning June 1, 1954, and secured by a third mortgage on its property. In consideration of these notes the payees surrendered to the corporation the debenture bonds for \$249,000 and the newly made promissory notes for \$26,829.28 and \$427,843.87.

By accepting the \$151,000 note in exchange for the two newly made promissory notes, the five former stockholders of Oregon Steel failed to recover \$303,625.90 of the total shown due from the corporation for their advances on open account, which at the time showed credit balances aggregating \$454,625.90. Pursuant to his agreement Morris Schnitzer made reimbursement to the other four in the amount of \$83,581.20 in order to reduce their loss to two-thirds of the total. This settlement was effected by a charge of that amount to Morris on the books of Alaska Junk and by his later delivery of second mortgage notes on account thereof to Alaska Junk. The charge of \$83,581.20 was explained in the journal as follows:

To charge Morris Schnitzer with  $\frac{1}{3}$  of total loss in steel mill deal. Total investment and a/c of A.J.Co. 727,032.13; total of Morris Schnitzer 163,993.77 or 891,325.90 for both—Total payment by mrtge 400,000. Total loss 491,325.90. Morris' share of loss  $\frac{1}{3}$  or 163,775.30. His investment and a/c of 163,993.77 less his interest in two mtge notes of \$83,799.67 results in loss of 80,194.10 on the amount he expended plus 83,581.20 due us.

Alaska Junk then charged off \$202,350.60 on its accounts with the corporation as a bad debt.

On October 3, 1943, the corporation's books indicated an operating loss to date of \$59,562.91. There were small operating losses in 1944 and 1945. For 1946 the books indicate a profit of \$278,196.85 before taxes. By 1947 corporate surplus exceeded a million dollars. Since November 26, 1943, and to the present time Oregon Steel has purchased large quantities of scrap from Alaska Junk.

Alaska Junk's partnership return for 1942 disclosed net profits of \$236,123.45, of which \$64,030.86 was reported as the distributable share of Sam Schnitzer; a like amount as the share of Harry J. Wolf, and \$54,030.86 as the distributable shares of each of their wives. Each of the four included such share in the income reported on his individual income tax return for 1942. Alaska Junk's partnership return for 1943 disclosed net profits of \$246,055.71, of which \$66,513.92 was reported as the distributable shares of Sam Schnitzer and Harry



J. Wolf and \$56,513.93 as the distributable shares of their wives. Each of the four included such share in the income reported on his individual income and victory tax return for 1943.

In computing the incomes of Sam Schnitzer and Harry J. Wolf for 1942 and 1943, the Commissioner denied recognition to the wives as partners for tax purposes, and included half of the partnership's net profits in the income of each of them. On the partnership's return for 1943 a deduction of \$202,350.60 was claimed as a bad debt, represented by Alaska Junk's open account with the corporation. The Commissioner disallowed this deduction. In the event that his failure to recognize Jennie Wolf as a partner should not be sustained, the Commissioner also determined a 1943 deficiency against her estate, computed to reflect her claimed share in the partnership income as recomputed by him. The Commissioner further determined Monte L. Wolf, Blossom M. Goldstein and Charlotte C. Cohon liable for Jennie Wolf's tax deficiency as transferees of her estate.

### Opinion

Johnson, Judge: After the Commissioner had recognized for many years that Rose Schnitzer and Jennie Wolf were members of the partnership conducting business under the style of Alaska Junk Co., he determined that for tax purposes, only their husbands, Sam Schnitzer and Harry J. Wolf, should be deemed partners in 1942 and 1943. He defends



that determination by the argument that the wives contributed no capital, rendered no services and exercised no control over the business; that the agreement of 1928, by which the husbands purported to transfer a one-fourth interest to each wife represents an attempt to divide income among family members; that the attempt was devoid of substance; reflected no bona fide intent to form a partnership with the wives, and should be ignored.

1. Petitioners contend that the wives' status as recognizable partners is *res judicata* and may not now be challenged. They cite this Court's opinion in their prior proceeding involving partnership income for 1941, and argue that the decision in their favor is conclusive of the issue here raised. Admitting, as they must, that the only error assigned related to the reasonableness of salaries, which the Commissioner had disallowed as a deduction in the computation of partnership profits for 1941, they insist that the Court's finding of an existing partnership comprising the wives "was not merely collateral or incidental, but was material," because the decision reached could not have been rendered without deciding that particular matter, and such matter was hence "properly within the issue controverted." *Packet Co. v. Sickles*, 5 Wall. 580; *Southern Pacific Railroad Co. v. United States*, 168 U.S. 1.

We are unable to accept this view. In the prior proceeding the wives' status as partners was admitted by respondent, not controverted. And while the prior

finding, based on the admission, is *res judicata* as to the parties' tax liability for 1941, *Cromwell v. County of Sac*, 94 U.S. 351, the present proceeding, involving tax liability for subsequent years, is based upon a different cause or demand. Under such circumstances the Supreme Court held in *Commissioner v. Sunnen*, 333 U.S. 591, that:

\* \* \* the prior judgment acts as a collateral estoppel only as to those matters in the second proceeding which were actually presented and determined in the first suit. \* \* \*

\* \* \*

\* \* \* If the legal matters determined in the earlier case differ from those raised in the second case, collateral estoppel has no bearing on the situation. See *Travelers Ins. Co. v. Commissioner*, 161 F. 2d 93. \* \* \*

Since the wives' status as partners was not placed in issue in the prior proceeding, it was not judicially determined. This is no less true because the uncontested finding was reflected in a computation of tax deficiencies under the decision rendered. *Pelham Hall Co. v. Hassett*, 147 Fed. (2d) 63; *Harvey Coal Corp. v. United States*, 92 Ct. Cl. 186; 35 Fed. Supp. 756; *C. D. Johnson Lumber Corporation*, 12 T.C.—(promulgated March 17, 1949). Accordingly, we hold that recognition of the wives as partners in this proceeding is not *res judicata*, and the doctrine of collateral estoppel does not preclude a determination of that issue on its merits now.

2. As an alternative to their plea of *res judicata*, petitioners contend that the evidence affirmatively establishes a genuine and recognizable intention of the husbands and wives to conduct the Alaska Junk Company's business as a partnership, and that they have overcome the respondent's contrary determination. They argue on brief that a partnership of the four was formed when the Schnitzers "managed to scrape together the \$1000.00" (which was 1911); later that "the partnership in fact dates from 1912 or 1913. The evidence of the exact date is conflicting"; that the wives initially contributed capital, small in amount but important at that time; that the instrument of 1928 merely recognized a pre-existing oral partnership agreement; that Jennie Wolf, being proficient in English and better educated, gave valuable aid to the business at the beginning and that both wives rendered services and exercised control by virtue of the husbands' deference to their judgment and that both were constantly consulted about business decisions and policy. Such participation, they conclude, meets every test which the Supreme Court considered pertinent in determining the *bona fides* of a family partnership in *Commissioner v. Tower*, 327 U.S. 280.

While petitioners' witnesses testified that a partnership of the four had existed since 1911, their statements are contradicted by their documentary evidence. Indeed the allegations of the petitions are to the contrary, for in them it is asserted that Sam Schnitzer and Harry J. Wolf engaged in a joint

venture in 1911; organized the Alaska Junk Co. as a corporation in 1912 with Horwitz, and upon its dissolution two months later Schnitzer and Wolf took over the assets and "entered into an oral partnership agreement." No mention is made of their wives, and prior to 1928 the wives filed no separate income tax returns. None of the four alleged partners testified, but their own understanding of their business relationship prior to 1928 is obvious from the language of the written agreement which all signed. In this they recite that the husbands "desire to admit" the wives as copartners in the business which "S. Schnitzer and H. J. Wolf have heretofore carried on." Such language not merely fails to recognize a preexisting partnership with the wives; it affirmatively refutes the witnesses' testimony that there was one. If a partnership of the four existed at all, it must have been created by the written agreement of 1928.

The recitations and provisions of that agreement disclose that the husbands transferred the two one-fourth interests "in consideration of love and affection." Petitioners do not assert that they contributed any capital then, but insist that in 1911 Schnitzer and Wolf were enabled to launch their business venture with marriage dowries, and these dowries, they contend, constituted a capital contribution by the wives.

In many prior decisions, holding a wife recognizable as a partner for tax purposes, substantial weight has been given to very small amounts of



capital contributed by her towards the development of the husband's business from humble beginnings, *Weizer v. Commissioner* (C.C.A., 6th Cir.), 165 Fed. (2d) 772; *Singletary v. Commissioner* (C.C.A., 5th Cir.), 155 Fed. (2d) 207; *Humphreys v. Commissioner* (C.C.A., 2nd Cir.), 88 Fed. (2d) 430; *Willis B. Anderson* 6 T.C. 956, even although she was not made a partner until later. *Canfield v. Commissioner* (C.C.A., 6th Cir.), 168 Fed. (2d) 907; *N. B. Drew*, 12 T.C. 5; *Paul L. Kuzmick*, 11 T.C. 288. Of necessity the evidence about the funds with which Wolf and Schnitzer began their independent operations is not detailed and precise. Harry J. and Jennie Wolf are deceased; Sam Schnitzer, being aged and ill, did not testify on advice of a physician. But an outline of the beginnings was given by sons, who knew it as a matter of family history, which testimony was received without objection from respondent. Both husbands at the time of their marriage in 1906 were poor, uneducated immigrants. Their wives brought each a dowry said to be about \$1,000, and aided each in starting business as an independent junk dealer in a humble way. Monte L. Wolf stated in general terms that the wives' dowries, at least in part, supplied the requisite capital, and attendant circumstances are very persuasive that this was so.

Respondent urges the technical objections that this fact is not established by competent evidence; that if true, it is wholly immaterial because of the short-lived corporation of 1912 which issued shares



only to the husbands and the ensuing partnership which was between them alone, and that absence of any agreement that the wives be partners is fatal. While such an agreement is necessary, *L. C. Olinger*, 10 T.C. 423, the requirement is adequately met by the subsequent instrument of 1928, and as is patent from the above cited cases, preceding capital contributions may properly be considered in deciding whether or not wives are partners recognizable for tax purposes by virtue of it. Perhaps standing alone, these early contributions would not be entitled to decisive weight. But they fit significantly into the accumulation of evidence that from the beginning and through the taxable years the wives took more interest in their husbands' business than may be regarded as a normal incident of the marital relation.

We have often rejected arguments that a wife is entitled to recognition as a partner because her domestic frugality, clerical aid, interest in business matters and home discussions influenced and assisted her husband in business operations. *John P. Denison*, 11 T.C. 686; *Edwin F. Sandberg*, 8 T.C. 423; *Floyd D. Akers*, 6 T.C. 693; *Leonard W. Greenberg*, 5 T.C. 732; *affd.* (C.C.A., 6th Cir.), 158 Fed. (2d) 800; see also *Bradshaw v. Commissioner* (C.C.A., 10th Cir.), 150 Fed. (2d) 918. But we are persuaded by the evidence before us here that the wives' participation in *Alaska Junk* greatly exceeded in extent and in degree of business character the services considered in such cases as those cited. *Jennie Wolf*,

in particular, with her better education and business acumen, appears to have exerted decisive influence over business discussions not only at the humble beginning when her husband was very dependent upon her, but increasingly over the years. Morris Schnitzer and Monte L. Wolf both testified that Wolf was dominated by her. The husbands took the wives with them on trips to investigate distant ventures for the benefit of the wives' opinions, and the wives' disapproval normally ended their interest in these projects.

On such a background the wives' failure to keep regular office hours, to have express authority to act for the partnership, or to hold separate funds loses its normal significance. Negotiations on important transactions and decisions about new ventures were made not at the office but at a partner's home with full participation of the wives. While as a book-keeping matter, the wives made no withdrawals of their credited shares of partnership income, in fact they took what they pleased, having their bills sent for payment by the partnership. And their participation in the undertaking of new ventures, in which the four and sometimes others had a share, was in effect a withdrawal by them of funds for investments in which they acquired a separate proprietary interest.

We find that the wives did contribute capital to the business in the beginning and that after being made partners in 1928, they rendered vital services and participated in control and management to a

degree which entitled them to recognition as partners for tax purposes. The Commissioner's determination to the contrary is accordingly reversed.

3. Petitioners assign error in respondent's disallowance of \$202,350.60 as a bad debt deduction from the partnership's profits for 1943. This amount is the difference between Alaska Junk's total advances to Oregon Steel, aggregating \$841,552.01, and total credits against such advances on the open account. The credits consist of \$124,900 for stock, \$174,000 for bonds, \$114,519.88 for repayments; \$142,200.33, allocated part of the \$151,000 note of the purchasers, and \$83,581.20 reimbursed by Morris under his guaranty agreement limiting loss. Although the disallowance does not plainly appear in any of the deficiency notices, which show merely an addition of partnership profits to the individual incomes of Sam Schnitzer, Harry J. and Jennie Wolf, all parties agreed in argument and brief that the \$202,350.60 was claimed as a bad debt deduction on the partnership return and that its disallowance is reflected in the determinations here in controversy. At the hearing respondent's counsel stated without contradiction that the Commissioner had treated the amount as a capital loss, and on brief contends that it should be so treated. We shall accept the parties' premises in considering the issue raised.

Petitioners argue that Alaska Junk's advances, over and above those applied on the books to payment for capital stock and bonds, constituted a loan

to Oregon Steel, made as an incident of the partnership's business of financing customers, and that the unrecovered portion of this loan, or \$202,350.60, remaining after sale of Oregon Steel's shares and the ensuing settlements in 1943, became worthless; was written off, and is deductible as a bad debt. Respondent argues to the contrary that the advances were investments in permanent assets of a new enterprise which required the full amount as capital; that the character of the advances as risk investment is indicated by the corporation's agreement not to make any payments to stockholders until the RFC loan should be fully discharged and by the stockholders' agreement among themselves that any losses resulting be borne by them proportionately to their holdings of corporate shares. Respondent also contends that even under the view that debts did result from the advances, they were not business debts, for Alaska Junk's occasional financial aid to customers and advances to other enterprises which the Schnitzer and Wolf families formed, did not constitute a business.

Whether a stockholder's advance of funds to his corporation is to be deemed a capital contribution or a loan is not a new question. It has arisen tax-wise in issues involving, as here, the proper treatment of unrecovered advances as a bad debt or as a capital loss deduction, *Maloney v. Estate of Spencer* (C.C.A., 9th Cir.), 172 Fed. (2d) 638; *Cohen v. Commissioner* (C.C.A., 2nd Cir.), 148 Fed. (2d) 336; *Van Clief v. Helvering* (D.C.App.), 135 Fed.



(2d) 254; *Woodward Iron Co. v. United States* (N.D.Ala.), 59 Fed. Supp. 54; *Edward G. Janeway*, 2 T.C. 197; *affd.* (C.C.A., 2nd Cir.), 147 Fed. (2d) 602; *Joseph B. Thomas*, 2 T.C. 193; *Glenmore Distilleries Co., Inc.*, 47 B.T.A. 213; *Harry T. Nicolai*, 42 B.T.A. 899; *affd.* (C.C.A., 9th Cir.), other point, 126 Fed. (2d) 927, and in issues involving a corporation's right to deduct amounts paid on such advances under the guise of interest, *United States v. South Georgia Ry. Co.* (C.C.A., 5th Cir.), 107 Fed. (2d) 3; *Commissioner v. Proctor Shop, Inc.* (C.C.A., 9th Cir.), 82 Fed. (2d) 792; *Swoby Corporation*, 9 T.C. 887; *Mullin Building Corporation*, 9 T.C. 350; *affd.* (C.C.A., 3rd Cir.), 167 Fed. (2d) 1001; 1432 *Broadway Corporation*, 4 T.C. 1158; *affd.* (C.C.A., 2nd Cir.), 160 Fed. (2d) 885; *Edward Katzinger Co.*, 44 B.T.A. 533; *affd.* (C.C.A., 7th Cir.), 129 Fed. (2d) 74. In *Talbot Mills v. Commissioner*, 326 U.S. 521; *Commissioner v. Schmoll Fils Associated, Inc.*, (C.C.A., 2nd Cir.), 110 Fed. (2d) 611, and *Commissioner v. O.P.P. Holding Corporation* (C.C.A., 2nd Cir.), 76 Fed. (2d) 11, a like issue was presented after exchanges of bonds for preferred shares, and the same question has arisen in bankruptcy proceedings. *Pepper v. Litton*, 308 U.S. 295; *Arnold v. Phillips* (C.C.A., 5th Cir.), 117 Fed. (2d) 497.

This question is one of fact. *Cohen v. Commissioner*, *supra*. And in deciding whether or not a debtor-creditor relation resulted from advances, the parties' true intent is relevant, *Fairbanks, Morse*



& Co. v. Harrison (N.D. Ill.), 63 Fed. Supp. 495; Edward Katzinger Co., *supra*; Daniel Gimbel, 36 B.T.A. 539. Bookkeeping, form and the parties' expressions of intent or character, the expectation of repayment, the relation of advances to stockholdings, and the adequacy of the corporate capital previously invested are among circumstances properly to be considered, for the parties' formal designations of the advances are not conclusive, *United States v. South Georgia Ry. Co.*, *supra*, but must yield to "facts which even indirectly may give rise to inferences contradicting" them. *Cohen v. Commissioner*, *supra*. See also *Commissioner v. Proctor Shop, Inc.*, *supra*. As the Supreme Court said, however, in *Talbot Mills v. Commissioner*, *supra*:

\* \* \* There is no one characteristic, \* \* \* which can be said to be decisive in the determination of whether the obligations are risk investments in the corporations or debts. So called stock certificates may be authorized by corporations which are really debts and promises to pay may be executed which have incidents of stock. \* \* \*

Viewing the complex history of Oregon Steel's organization and development, we are of opinion that the circumstances under which Alaska Junk made the advances require the conclusion that they were paid in as risk capital, not as a loan. The stockholders had every reason to believe as early as October, 1941, when Alaska Junk began to charge advances to the corporation's open account with it, that the authorized capital of \$250,000 (and a for-

tiori the \$187,800 par value of shares eventually issued) was only a fraction of the minimum requirements for construction of a steel mill. For this very reason the corporation was unable to procure commercial loans. Cost of the mill was estimated at \$987,035 in the MacDonald report of November 1941, which Morris Schnitzer submitted to the RFC; at \$1,050,000 in the second report submitted to the RFC, and at \$1,200,000 in the letter of Schnitzer and Wolf addressed to the RFC on December 1, 1942, on requesting approval of a \$700,000 loan. At that time the open account advances of Morris Schnitzer and Alaska Junk were already greatly in excess of \$187,800, the par value of issued stock, which petitioners would treat as the maximum capital invested, and in March 1943, when that amount was credited to the discharge of stock subscriptions, additional advances of \$249,000 were applied by credits to the purchase of corporate bonds, and even then there remained a balance of \$315,095.41 due Alaska Junk on the open account. The mill, however, was not ready for operation until June, and Alaska Junk continued to make large advances so that by November 26, 1943, their total from the beginning aggregated over \$800,000. Substantially all, with the possible exception of \$9,460 in iron scrap, had apparently been invested in the corporation's organization and plant, a permanent asset. Advances for such a purpose are by their very nature placed at the risk of the business, and if, as here, business operations have not even begun, we

fail to perceive any warrant for distinguishing a part of the advances on open account, avowedly credited to stock investment, from the remainder which were made, recorded, and used in exactly the same way.

Petitioners argue that large operation profits were reasonably anticipated and if they had been earned, the corporation could have repaid its other loans, which had priority, and also that part of the advances from Alaska Junk which had not been credited to stock purchase. In support they stress the mill's substantial earnings in recent years, and the unexpected difficulties which they encountered in erecting it. This argument lacks persuasive force. Even if the corporation had paid off the balance in its open account with Alaska Junk from earnings, such payment would have still partaken of the character of dividend distributions on risked capital invested in the plant. A corporation's financial structure in which a wholly inadequate part of the investment is attributed to stock while the bulk is represented by bonds or other evidence of indebtedness to stockholders is lacking in the substance necessary to recognition for tax purposes, and must be interpreted in accordance with realities. Cf. *Swoby Corporation*, *supra*; *Edward G. Janeway*, *supra*; *1432 Broadway Corporation*, *supra*. The testimony of petitioners' witnesses, especially Morris Schnitzer, that the shareholders never intended to invest more than \$187,800 in stock is intelligible only as showing an agreement about mere form.

But even form itself was not consistently observed. From incorporation on June 4, 1941, until sale of the shares on November 26, 1943, Alaska Junk and Morris Schnitzer made the advances on open accounts as funds were needed by Oregon Steel and were available or procurable by them. No advance, whether by cash payment, materials supplied or discharge of the corporation's bills and obligations, was specifically designated as made in satisfaction of a stock subscription, in payment for bonds, or as a loan. Throughout the whole period the advances were simply charged to open accounts receivable on the books of Morris Schnitzer and Alaska Junk and credited to open accounts payable on the corporation's books, and except for formal qualifying shares, no stock was even issued until February 10, 1942, and no record of payment for that was made until March 31, 1943. By the latter date the RFC loan had been approved; Wolf had objected to risking any more of Alaska Junk's funds in the enterprise, and a compromise agreement had been reached, basically changing stock ownership so that Morris Schnitzer would hold a third interest instead of a half and the other four, a two-thirds interest instead of a half. Then for the first time payments for shares, as redistributed, were indicated on the books of Morris and of Alaska Junk by credits to the corporation's open accounts with them in the par value amounts of the shares, not as issued, but as redistributed, to the several shareholders, and at the same time credits were made as



recording payment for \$249,000 in bonds simultaneously issued. There still remained over \$300,000 in the open account of Alaska Junk, which is reflected in the ultimate balance that petitioners now seek to characterize as a loan. On the corporation's own books corresponding entries were not made until July 14, 1943. And while, as petitioners' witnesses testified, the delay may have been due to the neglect of a bookkeeper, we can not but share the bookkeeper's probable feeling that the entries made little difference anyhow because the advances were all of the same character and could be distributed as desired among accounts for capital contributed, bonds issued and loans payable.

But any substantive effect that the parties' allocation of the advances among these three types of accounts might have is emasculated by their loan contracts and the agreement among themselves. So long as any part of the \$700,000 RFC loan remained unpaid, the corporation could not make payments on any account to the stockholders except \$15,000 annually as salaries; inventory and like assets, not covered by the RFC mortgage, were pledged to secure bank loans. Obviously in apprehension of losses, all five stockholders agreed that Morris Schnitzer should bear one-third and Alaska Junk two-thirds of total losses that might be sustained. Thus the proportion of risk fixed by the relative stockholdings was projected to cover all the advances and in the final settlement Morris paid Alaska Junk \$83,581.20 to reduce the partnership losses to two-



thirds of the total lost. The mere existence of such an agreement is incompatible with testimony that repayment of the advances was anticipated or with their characterization as loans. The stockholder had in view a nice matching of losses to the proportion of his corporate shareholding. Such a limitation is an incident of stock ownership, not of the debtor-creditor relation.

The closing entries, moreover, on the open account with Alaska Junk, recording the final settlement with Morris, refer to "total investment and a/c" and disclose that in computation of the amount due from Morris, the loss was computed on the basis of the total advances of Morris and Alaska Junk from the beginning, not the amounts in open account remaining after credits for stock subscriptions and bonds. In this and other written notations, the parties or their bookkeepers have made statements consistent only with the view that the advances were capital contributions. We feel that such characterizations in book entries, resolutions, applications and contracts are not ordinarily entitled to great weight in deciding such a question as that before us. But if, as here, they are numerous and consistent, and one is followed by a computation of "Total loss," in which all advances, whether attributed to stock, bonds, or loans, are indiscriminately grouped for arriving at a settlement among stockholders in the same proportion as their shareholdings, we must deem them a considered expression of the parties' own view.

Petitioners advert to repayments of \$114,519.88 on the account as supporting its loan character, but however significant this fact might normally be, the release of corporate funds to Alaska Junk, contrary to the RFC loan contract, was a special favor designed to aid Alaska Junk in desperate financial straits. And while the evidence does not set forth the details of such releases, it does show that Alaska Junk was unable to make advances for essential equipment or materials needed in mill construction and that RFC acted out of necessity. In substance it did no more than release a part of the \$700,000 loan for a specific purchase for the steel mill but through Alaska Junk.

We are of opinion that all of the advances were contributions to capital and that the ensuing worthlessness of a part thereof was not a bad debt. This conclusion makes it unnecessary to consider other contentions relative to business character of the alleged loan and its worthlessness.

Reviewed by the Court.

Decisions will be entered under Rule 50.

[Seal]

Served July 14, 1949.

The Tax Court of the United States  
Washington

Docket No. 14208

SAM SCHNITZER,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

DECISION

Pursuant to Opinion of the Tax Court promulgated July 14, 1949, the respondent filed a computation on October 6, 1949, and the petitioner, on November 7, 1949, filed an acquiescence in the computation as filed by the respondent. Now, therefore, it is

Ordered and Decided: That there is a deficiency in income and victory tax due from this petitioner for the calendar year 1943 in the amount of \$43,287.42.

/s/ LUTHER A. JOHNSON,  
Judge.

Entered Nov. 9, 1949.

Served Nov. 10, 1949.

In the United States Court of Appeals  
for the Ninth Circuit

T. C. Docket No. 14208

SAM SCHNITZER,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

### PETITION FOR REVIEW

Comes now the petitioner, by his attorneys of record, and respectfully shows this Honorable Court:

#### I.

The petitioner is an individual residing at 1011 S. W. Vista Avenue, Portland 4, Oregon. The returns for the periods here involved were filed with the Collector of Internal Revenue for the District of Oregon.

#### II.

The respondent is the duly appointed, qualified and acting Commissioner of Internal Revenue of the United States and is hereinafter referred to as the "Commissioner."

#### III.

The taxes in controversy are income and victory taxes for the calendar year 1943.

## IV.

## Nature of Controversy

For many years prior to and during the taxable year before the court Sam Schnitzer, Harry J. Wolf, Rose Schnitzer and Jennie Wolf were doing business as copartners under the name and style of Alaska Junk Company. During the years 1942 and 1943 Alaska Junk Company was engaged in the business of buying, selling and generally dealing in junk, pipe, tools, machinery, hardware, scrap and other metals and, as a part of its regular business, made loans and advances to customers and affiliated enterprises, always treating these loans and advances as "accounts receivable" on its books of account.

Morris Schnitzer, a son of Sam Schnitzer, was engaged in a similar business and in 1941 organized the Oregon Electric Steel Rolling Mills (hereinafter referred to as "Oregon Steel") an Oregon corporation, to manufacture steel products. The company's authorized capital was 2,500 shares having a par value of \$100.00 each, a total capital of \$250,000.00. Upon final distribution of this stock the partners of Alaska Junk Company received 1,249 shares and Morris Schnitzer 625 shares.

From October, 1941, to November, 1943, Alaska Junk Company advanced to Oregon Steel, cash \$327,870.23, paid bills of \$166,340.16 and furnished goods at market prices to the amount of \$347,341.62, making a total of \$841,552.01. All of these items



were charged on Alaska Junk Company's books as "accounts receivable" from Oregon Steel. On the books of Oregon Steel these items were entered as "accounts payable." Alaska Junk Company received payments of cash \$114,519.88, received stock of a par value \$124,900.00 and debenture notes of a face value of \$174,000.00 making total receipts of \$413,419.88, which items were credited to said accounts receivable.

Morris Schnitzer and Alaska Junk Company orally agreed that Morris Schnitzer would bear  $\frac{1}{3}$  of the total loss, if any, that might be sustained by Morris Schnitzer and Alaska Junk Company from advances to Oregon Steel over and above the advances credited to stock subscriptions. Alaska Junk Company in turn agreed to bear  $\frac{2}{3}$  of any such loss.

Alaska Junk Company was induced to make the advances, sell goods on credit and pay the bills of Oregon Steel upon a promise of early repayment, based upon engineering estimates of minimum earnings of \$50,000.00 per month and a production schedule to begin early in 1943.

In June, 1943, Morris Schnitzer was inducted into military service and Oregon Steel was unable to obtain competent management. As a result of this and other difficulties the operations were unsuccessful, and in November, 1943, ceased. It was then decided by the stockholders to withdraw from the enterprise, and Oregon Steel stock was then sold. Prior to the sale Oregon Steel issued Alaska

Junk Company its promissory note for \$427,843.87, the balance of its account receivable, and issued its note of \$26,829.28 to Schnitzer Steel Products Company (Morris Schnitzer). In exchange for these two notes Alaska Junk Company and Morris Schnitzer received a third mortgage note for \$151,000.00. This compromise resulted in a total loss of \$303,625.90 and by reason of the agreement between Morris Schnitzer and Alaska Junk Company, Alaska Junk Company sustained a loss of \$202,350.60, which was charged off as a bad debt. On the partnership's return for 1943 a deduction of the \$202,350.60 was claimed as a bad debt. It is this amount which the Commissioner has disallowed as a deduction. The Commissioner's contention was upheld by the Tax Court of the United States and petitioner submits that in making its determination the Tax Court was in error.

## V.

The petitioner designates the following points on which he intends to rely on appeal to the United States Court of Appeals for the Ninth Circuit from the decision heretofore entered by the Tax Court of the United States:

1. The Tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the partnership in which petitioner was a partner was not deductible as a bad debt in computing petitioner's own net income subject to taxation.

2. The Tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the part-

nership in which petitioner was a partner was not a bad debt.

3. The Tax Court erred in holding that all of the advances, including said sum of \$202,350.60, of the partnership in which petitioner was a partner were contributions to capital.

4. The Tax Court erred in not finding and holding that all of said sum of \$202,350.60 was a loan made by the partnership in which petitioner was a partner.

5. The decision entered by the Tax Court herein is not supported by the evidence, is contrary to the evidence and is in disregard of it.

6. The Tax Court erred in determining that there was a deficiency in income and victory taxes for the calendar year 1943 due from the above-named petitioner.

Wherefore, the petitioner petitions that the decision of the Tax Court of the United States be reviewed by the United States Court of Appeals for the Ninth Circuit; that a copy of the record on review be prepared in accordance with law and with the rules of said Court and transmitted to the Clerk of said Court for filing and that appropriate action be taken by said Court to review and correct the decision of the Tax Court which petitioner submits is erroneous.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,

Attorneys for Petitioner.

Received and filed T.C.U.S. January 4, 1950.

[Title of Court of Appeals and Cause.]

NOTICE OF FILING OF  
PETITION FOR REVIEW

To: Charles Oliphant, Chief Counsel for the  
Bureau of Internal Revenue.

You will please take notice that on the 4th day of January, 1950, the petitioner above named filed with the Clerk of the Tax Court of the United States at Washington, D. C., a Petition for Review by the United States Court of Appeals for the Ninth Circuit of the decision of the Tax Court of the United States heretofore entered in the above-entitled proceeding.

A copy of said Petition for Review as filed is attached hereto and served upon you.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES.

Personal Service of the foregoing together with a copy of the Petition for Review is hereby acknowledged this 9th day of January, 1950.

/s/ CHARLES OLIPHANT, C.A.R.

Chief Counsel, Bureau of Internal Revenue, Counsel  
for Respondent.

Received and filed T.C.U.S. January 9, 1950.

The Tax Court of the United States  
Docket Nos. 14208, 14209, 14278, 14279, 14280, 14372

SAM SCHNITZER, HARRY J. WOLF, MONTE  
L. WOLF, BLOSSOM M. GOLDSTEIN,  
CHARLOTTE C. COHON, ESTATE OF  
JENNIE WOLF,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

June 10, 1948, 9:30 a.m.

(Met, pursuant to notice.)

Before: Honorable Luther A. Johnson,  
Judge.

Appearances:

RANDALL S. JONES, ESQ.,  
917 Public Service Bldg.,  
Portland, Oregon,

ROBERT T. JACOB, ESQ.,  
917 Public Service Bldg.,  
Portland, Oregon,

Appearing for the Petitioner.

LEONARD ALLEN MARCUSSEN, ESQ.,

Appearing for the Respondent. [1\*]

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\* Page numbering appearing at top of page of original Reporter's Transcript.



REPORTER'S TRANSCRIPT OF RECORD

\* \* \*

Whereupon,

MORRIS SCHNITZER

a witness called by and on behalf of the Petitioner, having been first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Jones:

Q. Will you state your name?

A. Morris Schnitzer.

Q. Were you the president of the Oregon Electric Steel Rolling Mills; is that the correct name?

A. Yes.

Q. You were the president? A. Yes.

Q. From now on, in referring to it, I will say "Oregon Steel" only. Where did you attend school? A. University of Washington.

Q. What was the course that you took? [32]

A. Engineering, and one year of business administration.

Q. During the summers and during your vacations, in what did you engage?

A. I worked at the Alaska Junk Company.

Q. And after you finished school and until after you entered into the Oregon Steel, what did you do?

A. I continued the work at the Alaska Junk there.

Q. For how long?

A. I was with the Alaska Junk after I finished college, until 1934, I believe.

(Testimony of Morris Schnitzer.)

The Court: When?

The Witness: The first part of 1934.

Q. (By Mr. Jones): Were you ever a partner of the Alaska Junk before 1943?

A. Yes, I was a partner with *the* on some ventures. In 1932 up to and including 1934.

Q. My question is, were you ever a partner in the Alaska Junk Company itself?

A. No, sir, I was not.

Q. Explain the ventures which you mentioned?

A. On outside work, where I was completely away from any interest in the Alaska Junk Company, we made a gentlemen's agreement, between Mr. Wolf and Mr. Schnitzer and myself, in [33] which I was to receive one-third of all the profits of my own work, as such, a venture that went on for a little over two years.

Q. Where was that?

A. Down at Marshfield, Coos Bay, and Reedsport, Oregon.

Q. What did it consist of?

A. I had bought three or four railroads; I bought all the tracks and the rail and the equipment at the company's jobs at Coos Bay, and on the Umpqua, and, in turn, bought and sold a lot of machinery and equipment down there.

Q. About when did that start?

A. It started in 1933.

Q. What part of 1933?

A. It was toward the end of 1932 and the first of 1933.

(Testimony of Morris Schnitzer.)

Q. And when did you finish down there?

A. I finished that venture about January or February of 1934.

Q. Then where did you go?

A. I severed my relationship with the Alaska Junk Company and went to California, and from there I had several jobs in New Orleans and Arizona. I bought some big steel jobs, plants, and wrecked them.

Q. What kind of jobs?

A. Refineries, copper smelters, and I also handled a [34] railroad job in California, and a sawmill job in California.

Q. What did you do with those railroad jobs and sawmill jobs?

A. Well, I bought the complete assets, that is, the rails and equipment and everything.

Q. And you sold them for scrap?

A. Yes, for scrap or relayers in the case of rails.

Q. When did you return to Oregon?

A. I returned to Oregon in the summer of 1935.

Q. And where did you go then?

A. I leased ten acres down at the Guild's Lake area, and decided to build a plant for myself.

Q. What kind of a plant?

A. A scrap and field steel yard.

Q. What was the name of the yard or company?

A. Schnitzer Steel Products.

Q. Who are the owners?

(Testimony of Morris Schnitzer.)

A. I control ninety-eight per cent of the stock today.

Q. It is a corporation?

A. It is today, yes.

Q. Was it in 1941 and 1942 and 1943?

A. No, sir.

Q. Was it before that?

A. No, sir; it operated under an assumed name certificate. [35]

Q. Now, after your venture around Marshfield, did you ever work as an employee after that for Alaska Junk Company?      A. No, sir.

Q. Then, all of your connections, except in buying and selling, or going into the joint ventures, or owning stock in the same company, so far as the Alaska Junk Company was concerned, stopped when you went to Marshfield?

A. That is true.

Q. Now, would you mind telling us how you came to start the Oregon Steel? Where were you when you got the idea?

A. I had just about completed dismantling a wreck on Treasure Island, after grounding. We completed our job and sold the balance of it to the Navy. As a boy, of course, being in the steel business, we also knew the steel jobbing and the steel scrap business; and we had some contact with steel mills, and there always had been a dream of my father's that he would like to have a small steel mill. I had the opportunity at the time; I was

(Testimony of Morris Schnitzer.)

free, and no large work ahead; I thought that was the right time to go ahead, knowing the industry work was rapidly expanding; therefore I thought it was a good time to go ahead.

Q. Where were you at that time?

A. I was at San Francisco.

Q. Did you have a corporation then organized?

A. Yes; I wrote to my attorney here and asked him to [36] organize a corporation.

The Court: When was the corporation organized?

The Witness: About the first day of June, 1941.

Mr. Jones: Now, if your Honor please, that is in the stipulation; and the stock arrangement.

The Court: That is fine.

Q. (By Mr. Jones): You subscribed, the stipulation shows, to 1251 shares. Why did you subscribe to that amount?

A. Well, for one thing at that time I wanted to have control of the corporation. I had definitely no exact amount of the cost of the company, and at least during the initial stages I wanted to know what was going on and I wanted the control of it.

Q. Now, after your original stock subscriptions, where you took that amount, and the partners of the Alaska Junk Company took 625, and then re-allocated it amongst themselves, was there any other agreement about stock ownership?

A. What do you mean?



(Testimony of Morris Schnitzer.)

Q. About how you would make interchanges in your stock interests?

A. I don't get that question.

Q. The stipulation shows that you first had 1251 shares? A. That is right.

Q. And then subsequently had 625 shares issued to the [37] partners of Alaska Junk?

A. That's right.

Q. What was the agreement and the understanding that caused the reissuance of the stock?

A. I think you are off there. Originally it was 1251 and 625. That was the basis of two-thirds and one-third. Is that what you are asking?

Q. No. I asked you after you subscribed to 1251 shares and the Alaska Junk partners took 625, how it came that they took part of theirs—rather, a part of yours; they took half of yours later, did they not?

A. Now you are talking about later on?

Q. Yes.

A. That is a lot different than the question you asked me. The reason I could not handle the balance of the money that was involved was this: in the course of construction they advanced more money in proportion to the one-third than they were supposed to, to the end that Mr. Wolf asked for a realignment or readjustment of the stock on the basis of the amount of money that was due them, with the result I had to give them one-half of my stock, or 1251 shares, and I only kept one-third and they kept two-thirds.

(Testimony of Morris Schnitzer.)

Q. Of the issued stock?

A. That is right.

Q. About when did that happen?

A. That took place about the first of January, 1943. [38]

Q. And during these conversations was there any guarantee of any kind made between you and the partners of Alaska Junk?

Mr. Marcussen: I will object to that on the ground that there is no testimony about any conversation. Could we have the conversations identified.

Q. (By Mr. Jones): First, I would like to know about the agreement——

Mr. Marcussen: My objection is to any conversation before it has been established there was any.

Mr. Jones: Will you read the question?

(Whereupon, the question referred to was read by the reporter as follows: "And during these conversations was there any guarantee of any kind made between you and the partners of Alaska Junk?")

Mr. Marcussen: I didn't get your questions of conversations as directed to the guarantee.

Mr. Jones: Yes.

Mr. Marcussen: The objection is withdrawn.

A. Yes; I did guarantee Alaska Junk; and that was due to the fact that at this time the Alaska Junk had put so much money ahead of my investment that Mr. Wolf got leery and didn't want to

(Testimony of Morris Schnitzer.)

advance any more money or material. We made an arrangement that I would give one-half of my stock, and I guaranteed that I would take care of my end of the one-half of [39] the loss; I guaranteed, in the case of any losses, that I personally would pay the difference to the Alaska Junk on account of any advances in merchandise.

Q. How was that guarantee to operate? You say you had one-third? One-third of what?

A. Let me put it simply: in case the Alaska Junk should take any losses for advances, and so forth, over and above their proportionate advances, in proportion to the reissue of the stock, that is, two-thirds of the investment and I having one-third of the investment; in other words, the losses, if any, would be borne in proportion to the stock we had.

The Court: Tell us how you guaranteed it?

The Witness: Just as I stated.

Q. (By Mr. Jones): I asked you this question, what was the basis? You said you guaranteed one-third. I asked you, you guaranteed one-third of what?

A. Of their losses and my losses combined. I guaranteed that the difference, if I lost and they should lose, that Alaska should be repaid anything that was in excess of the two-thirds of the losses incurred by both of us. I guaranteed the difference between one-third and what the actual figure was; in other words, my loss would be a full one-third

(Testimony of Morris Schnitzer.)

and their full loss would not be more than two-thirds. If it was, I would pay that difference. [40]

Q. On what kinds of accounts did this guarantee operate? What kind of losses are you speaking of?

A. This was on the open books.

Mr. Marcussen: I have an objection, if your Honor please, that this calls for a conclusion of the witness, and move that it be stricken as to whether it was an open book loss or not. That is a conclusion of the witness.

The Court: I think he would be entitled to show what interest each one had. I think it is a part of the explanation. I will overrule the objection.

Q. (By Mr. Jones): Did you ever talk with any of the partners of Alaska Junk about how much they would invest in the capital of the Oregon Steel?

A. Yes, we had many discussions on that. Of course, the whole picture—I think, in all fairness to everybody, this plan or unit was promoted on my idea. I started working on it in 1941, at which time costs were very much lower than they were in 1942 and 1943 or 1944. I think, in all fairness, we made three engineering reports, three different engineering reports, at different times, and at each time each report was a little higher. We never intended to invest so much capital.

Mr. Marcussen: Just a minute. Before we go too far. He has asked him to state what conversation he had with [41] the parties involved pertaining



(Testimony of Morris Schnitzer.)

to the investment in capital, and I think the answer should be confined to that.

The Court: I think there is an issue involved as to whether or not it was a capital loss, and I think perhaps intention might be material. I will overrule the objection.

A. (Continuing): Well, in this picture here, I had to spend two years in Washington, D. C., trying to get money, trying to get the plans started, and all this time—I would say this, that our financial statements at the time are on record, not only in the banks but in Washington, D. C.; and the amount of capital that we could have put in has never been altered. I don't think we made any statement anywhere that we ever intended to put in over \$187,000.00 capital stock.

Q. (By Mr. Jones): My question went to what the conversation was with the partners of Alaska Junk with respect to what Alaska Junk would put in?

A. I think that is answered by the fact that Alaska Junk, the last six months or a year of this whole thing,—we never knew ourselves until the last minute; we didn't want to put any more money in than we had to.

Q. Was there ever in your agreement,—was there ever a limit set in your agreements with Alaska as to what they would put in?

A. As to what Alaska's share in the subscribed capital? [42]



(Testimony of Morris Schnitzer.)

Q. As to what it would be?

A. The maximum was two-thirds.

Q. Of the subscribed stock?

A. Of the subscribed maximum. I would not say two-thirds. No. Mr. Wolf never wanted to put in any more than \$125,000.00 towards capital.

Q. Did he ever say so? A. Yes.

Q. You heard him? A. Yes.

Q. There were 622 unissued shares; why were they not issued?

A. At the time this company was formed we had a man in New York by the name of Mr. Rosenbaum who was given some money for helping us, and he was promised a sum of money for this stock, and that was somewhere around twelve and one-half per cent.

The Court: Will you state that again, please?

The Witness: A gentleman in New York was offered some stock for his services. We had to keep some open for him; we had, in the two or three year period approached other people and investment men, and as in the case of Mr. L. G. Knight of Seattle,—we wanted to get him in the operation, that is, to come in with an interest in stock; we wanted him to come in and operate the company. [43]

The Court: May I have the answer read?

(Whereupon, the last answer was read by the reporter as above recorded.)

Q. (By Mr. Jones): How was this stock allo-

(Testimony of Morris Schnitzer.)

cated? Did you have any plan at this time as to how those 622 shares would be paid for, if they were issued to someone?

A. That stock which would be issued to Mr. Rosenbaum would be charged as a promotion in the formation of the company.

Q. Did he assist in that? A. Yes.

Q. And the stock for Knight?

A. I believe Mr. Knight's stock was to be handled this way, that he would pay for some and be given an opportunity to pay for the balance out of the salaries and proceeds or profits.

Q. And neither man received any stock?

A. Neither man, of course, did.

Q. How much was to be held out for Rosenbaum?

A. About twelve and a half per cent, I believe.

Q. That would be about 312½ shares, wouldn't it? A. I think so.

Q. What was to happen to the others? Was the other block of shares what Mr. Knight was to get? A. That is right. [44]

Q. If he did not take it all, and you issued the rest, what was the plan?

A. Whoever got it would have to pay for it.

Q. Whoever was going to get it would have to pay for it? A. That's right.

Q. And if you wanted it, you would have to pay for it?

A. If I wanted it, yes. You are asking what was the plan.

(Testimony of Morris Schnitzer.)

Q. Were you giving it away?

A. We had no intentions of giving it away at any time. We did not intend to.

Q. You did not?

A. No; we never intended at that moment to give it away.

Q. At that moment. Did you ever intend at any time?

A. If I gave it away, I certainly would get services or cash or something in return.

Q. In other words, the company was going to sell it? A. Yes, that is right.

Q. When you finally got your 1942 plans, did the mill cost more than the estimate?

A. Just what do you mean?

Q. There was an estimated cost for the plant; did the mill cost more than the 1942 estimate?

A. It did. [45]

Q. By about how much?

A. By about three hundred fifty or three hundred seventy-five or four hundred thousand dollars.

Q. Was there any restriction of any kind placed upon the corporation, upon Oregon Steel, with respect to paying either yourself, that is, yourself as an individual, or Schnitzer Steel Products or Alaska?

A. Well, the R.F.C. put a restriction on, as far as my salary was concerned; they only would let me draw \$15,000.00 a year out of the business.

Q. What was the restriction about paying the open account?

(Testimony of Morris Schnitzer.)

A. So far as the open accounts were concerned, the R.F.C. man or representative there, Mr. McGonagle, refused to let our office at the steel mill pay the Alaska Junk or myself for the open account.

Q. Is that the reason why the open account got to the size that it did?           A. Yes.

Mr. Marcussen: I will object to that as calling for a conclusion of the witness, and ask that the answer be stricken.

The Court: Overruled.

Q. (By Mr. Jones): Who was Mr. McGonagle?

A. He was an engineer brought out here by the Reconstruction Finance Corporation, who had had some large plants built under his control with the R.F.C. and the D.P.C. He was the engineer in charge of keeping contact and watching our operations for the R.F.C., and in charge of expenditures.

Q. When were you first notified by the Draft Board?

A. Well, of course I registered and I got my first notice somewhere around June of 1942. I got by on that until my second notice in February of 1943.

Q. And when were you finally inducted?

A. I was inducted the last week of June of 1943.

Q. How long were you in the army?

A. Two and one-half years.

Q. Inducted June, 1943?

(Testimony of Morris Schnitzer.)

A. I believe the exact date was June 22 or June 23. They gave me ten days' notice.

Q. Where did you spend the greater part of your time in the army? A. In Europe.

Q. When did you return?

A. November of 1945.

Q. What was your grade when you returned?

A. Sergeant.

Mr. Marcussen: I will object to that as having no materiality; I am willing to stipulate that this man has performed [47] his duty to his country.

The Court: I don't think that is material. What did you ask him?

Mr. Jones: I asked him what his grade was when he returned.

Mr. Marcussen: His rank?

Mr. Jones: Yes.

The Court: I will overrule the objection. What was the answer to the question?

The Witness: Sergeant.

Q. (By Mr. Jones): When you went into the steel mill, did you have any estimate of what the probable earnings would be as soon as it got into production?

A. The estimate by the best and most capable engineers was that this plant would earn between \$60,000.00 and \$75,000.00 a month on a two-furnace operation.

Q. Of your knowledge, do you know of any



(Testimony of Morris Schnitzer.)

other businesses that the Alaska Junk helped to finance?

A. Yes; they helped me in 1939 to start the Industrial Air.

Mr. Marcussen: I will object to the question. Oh, I will withdraw the objection.

The Witness: They helped me in 1939 to start the Industrial Air Products Company. I also know of their starting [48] the National Machinery Company, because at that time I was very much interested in the company. I also knew of the Central Plumbing or Central Supply.

Q. Do you know whether they made any advances to those companies?

Mr. Marcussen: I will object to the question on the ground that the witness is not qualified, and not the best evidence.

The Court: I think that should be shown by a better source. The objection is sustained.

Q. (By Mr. Jones): When you went to the army, did you leave any power-of-attorney?

A. Yes, I left a power-of-attorney with my father, Sam Schnitzer.

Q. And he could act for you on anything in the steel mill during your absence? A. Yes.

Q. Well, do you know whether there was anyone in your family or in the Wolf family that had had any experience in steel making or in the operation of a furnace or rolling mill?

A. Well, there was no one, sir. [49]

(Testimony of Morris Schnitzer.)

Q. (By Mr. Jones): On this guarantee that you spoke about with the Alaska Junk, did they make any guarantee back to you? In other words, was it a two-way guarantee? A. Yes.

Q. How did it work, so far as you were concerned?

A. So far as I was concerned, I had to pay quite a bit of money to balance the debt that they had incurred.

Q. If it had been the other way, did they have to [57] guarantee you that your losses would not exceed a certain amount?

A. My full one-third?

Q. That your losses would not exceed one-third?

A. That is right.

Q. At what prices, when Oregon Steel bought from Alaska—what prices did you pay to Alaska for merchandise out of their stock?

A. We paid the standard prevailing price.

Mr. Marcussen: I will object to that on the ground that the witness has not been shown to be qualified to testify about the prices paid for scrap. There is no indication in that regard that any scrap was sold to Oregon Steel when he was connected with it.

The Court: Find out if any was sold, at any time when he was present, or when.

Mr. Marcussen: That is the point of my question.

The Court: Let us find out whether there was any transaction.

(Testimony of Morris Schnitzer.)

Q. (By Mr. Jones): Keep out the scrap that was purchased after you went away, and I want to call your attention to the things that were purchased for the construction of the mill before you went into the service; do you know on what basis or on what price that merchandise was purchased?

A. We paid the standard prices for what was purchased, which standard prices were gauged by the Moore Book, which was the book that the Portland Jobbers Association paid, or which they went by. That was for scrap. For new steel that was fabricated, we paid the jobbers' price; for electric motors and so forth, the same.

Q. When they purchased for you on the outside from third party vendors, what did they charge you?

The Court: What do you mean by "they"?

Mr. Jones: The partners at the Alaska Junk Company.

Q. (By Mr. Jones): When they made purchases for you or paid bills for what you purchased, do you know what they charged, or whether they charged any profit on those transactions?

A. There was no profit, sir.

Mr. Jones: You may cross-examine.

Mr. Marcussen: If your Honor please, may we have a brief recess for about ten minutes?

The Court: Yes.

(Testimony of Morris Schnitzer.)

(Recess.)

Mr. Jones: I have one or two more questions, if your Honor please.

The Court: Go ahead.

Q. (By Mr. Jones): This man Rosenbaum that you spoke of, what was his [59] function in this thing?

A. In 1941 I went to New York to try to get this promoted in Washington, and also to help get this plan financed; and there was a period of about six months in which I worked with him.

The Court: With whom?

The Witness: With this man Rosenbaum in New York. I went to private capital in New York, and also to the R.F.C. in Washington. We worked together on the O.P.M., prior to the War Production Board, on promotion, to build the plant; and he did serve some functions.

Q. (By Mr. Jones): Did he ever give you any advice with respect to the capitalization of the Oregon Steel?

A. Yes; our original application to the R.F.C. was made—we sought his advice at that time.

Q. To the extent of what the capital stock structure should be?

A. Yes, he was here; he made a trip here and stayed at the Benson Hotel in, I believe, it was July or the first part of August of 1941. I am not quite positive on that date. But he was here in con-

(Testimony of Morris Schnitzer.)

junction of setting up the capital stock of the Oregon Electric Steel Rolling Mills.

Q. What capitalization did he recommend to you?      A. \$250,000.00. [60]

Mr. Marcussen: What was that?

Mr. Jones: I asked him what was the capitalization his financial advisor recommended. That is all. You may cross-examine.

### Cross-Examination

By Mr. Marcussen:

Q. Did Mr. Rosenbaum give a report to you?

A. We had mail from him; we never actually got a report.

Q. Did you ask him to make a survey?

A. No, we did not. What kind of a survey do you mean?

Q. As to what it would cost to construct it?

A. Yes, he advised us to go to McDonald Brothers in New York. We did, and they made an original survey and report on this plant.

Q. Mr. Rosenbaum did not make any survey?

A. No sir, he did not.

Q. How long was he here in Portland at the Benson Hotel.      A. One day.

Q. Was he here on your invitation?

A. No, he was not. I believe he had some business in Seattle, and he stopped one day here and then he returned to New York.

Q. How did you know of his presence here in Portland? [61]



(Testimony of Morris Schnitzer.)

A. He informed me he was coming west.

Q. What was the occasion for his informing you?

A. To work on this capital stock structure.

Q. Had you requested him to do that?

A. Had we requested him?

Q. Yes.

A. Yes, we did. We asked his advice on that.

Q. Did you write him a letter?

A. There was a lot of correspondence back and forth.

Q. Who signed the letter?

A. On most of the mail, I did.

Q. Where are those letters now?

A. Which letters, sir?

Q. The letters to Mr. Rosenbaum?

A. He has got some of them, I guess.

Q. Do you have copies of them?

A. Our copies, most of our attorneys have them, sir.

Q. Do you recall when you first wrote him?

A. I first wrote him in early 1941.

Q. Do you recall the nature of your statement in that letter?

A. I recall some of the statements, yes.

Q. What was the substance of the letter?

A. That we wanted to build a steel mill, and he wrote us back that he had conferred with his man Harry Neider. [62]

Q. What did you say besides telling him that you were going to start a steel mill?

(Testimony of Morris Schnitzer.)

A. I cannot tell you.

Q. What was the occasion of informing him of that fact?

A. We were trying to work out a steel mill.

Q. What did you ask him to do about it? Why did you consult him about it?

A. About the financing, sir.

Q. What was the date of your inquiry?

A. I cannot tell you the date without checking the actual letters.

Q. What was his reply?

A. His reply was that he would like to have me back in New York to talk the thing over, and he thought it could be worked out.

Q. Did you go to New York to see him?

A. Yes.

Q. About when was that?

A. That was in the early part of 1941; that was the early part of 1941, somewhere around May, I believe; no, I will take that back, sir. It was in June. I was back there in June.

Q. Was it before or after the organization of the corporation? [63]

A. I really could not tell you about that without checking.

Q. How long were you in New York on that occasion? A. I think it was about ten days.

Q. What were you doing there at that time?

A. I had gone to Washington, D. C., to check up on some of the possibilities of getting the thing

(Testimony of Morris Schnitzer.)

through the O.P.M., and, also, checking on the availability of some of the equipment, and also talking with Mr. Rosenbaum.

Q. How much time would you estimate was spent with Mr. Rosenbaum?

A. Well, I made several trips there at which time I spent a week or ten days. I was in the East off and on for a year during that time.

Q. I am talking about your trip in early June. I understood it was your testimony that you were there for about ten weeks on that occasion.

A. I think that is about right.

Q. Do you mean to say you were in New York all the time?

A. No, I went back and forth between Washington and New York. I was in Washington a part of that time.

Q. Well, about how much of your time were you in New York?

A. A couple of days in New York. [64]

Q. Did Mr. Rosenbaum go to Washington with you? A. No sir.

Q. Where were your conferences with him? Were they at all times in New York?

A. In his office.

Q. In his office in New York? A. Right.

Q. What was his business?

A. Promoting; I think that, basically, answers it. He is supposed to be a financial wizard.

Q. Of whom did you learn that?

(Testimony of Morris Schnitzer.)

A. Through this relative, Harry Neider, who lived in Seattle.

Q. By "promoter," you mean he would get new business enterprises started?

A. I wouldn't say that he could get them started.

Q. Well, does he finance them?

A. He has no money; I don't know how much money he actually has of his own, but so far as using his own money for financing, that is not his game. He took me down to two or three Wall Street outfits who were not interested; the trips did not prove fruitful.

Q. Did you ask him at any time whether he could raise any capital for you or any money for this enterprise that you had in mind? [65]

A. Yes, we did.

Q. Who were the organizations, or what were the organizations that he took you to in New York?

A. We went to the Hartley Rogers Company.

The Court: Did you mean Mr. Rosenbaum went with you when you said "we"?

The Witness: Mr. Rosenbaum took me to Hartley Rogers and to Commercial Credit. Hartley Rogers promote stock issues, and Commercial Credit loans money to businesses.

Q. (By Mr. Marcussen): Where are their offices in New York, if you recall?

A. I don't recall, sir. Hartley Rogers are on Wall Street, and Commercial Credit are up somewhere on 34th.

(Testimony of Morris Schnitzer.)

Q. Did Mr. Rosenbaum introduce you at Commercial Credit and at Hartley Rogers?

A. Yes.

Q. By the way, were there any financial houses, any other financial houses that he took you to?

A. Those were the only two.

Q. Those were the only two?

A. Yes, in New York.

Q. What did Mr. Rosenbaum say was his purpose in taking you to these organizations?

A. Well, he was trying to see if he could arrange capital to finance it. [66]

Q. Money to invest and to put into the business?

A. Yes.

Q. What was the outcome at Hartley Rogers?

A. They were not interested in the deal.

Q. Why not?

A. There was no engineering report or anything on the plan. They had, I believe, at that time—I think at Hartley Rogers they said they couldn't sell any stock of this kind on the market without any previous past experience.

Q. What was the outcome at Commercial Credit?

A. Commercial Credit could not advance us any money on this deal.

Q. What was the reason that was given that they could not advance any money on the deal?

A. The same thing; they had no engineering report on the plan, and the amount of capital which we told them we could put in as a maximum, which



(Testimony of Morris Schnitzer.)

they said was not enough; the amount of capital that we were to put in and the amount that we wanted from them; they said our ratio was too small an investment.

Q. That is, the ratio of your investment to the total?      A. That's right.

Q. Did they say something also about it being a new enterprise, and they would not be in a position to, or would not take stock in a new and unproven enterprise? [67]

A. Commercial Credit would have if we had put more money into it. In other words, if we put in a lot of money, they would give us a mortgage on it.

Q. Did you tell them that you were limited to \$250,000.00 capital which had been authorized?

A. That is right; very definitely.

Q. And that was all the capital stock that you intended to authorize for the organization?

A. That is right.

Q. Did you tell them then whether or not—did you tell them how much you intended to issue of the capital stock?

A. We told them it would be a maximum capital of \$250,000.00.

Q. Did they tell them at that time that you intended to secure a loan from the Reconstruction Finance Corporation?

A. Yes, we told them both at that time that we would try to, or were going to make a request for a loan.

(Testimony of Morris Schnitzer.)

Q. Did that fact change their minds any about their position?      A. No.

Q. Now, what other establishment did Mr. Rosenbaum take you to?

A. The MacDonald Brothers Engineering Company.

Q. Where is the MacDonald Brothers Engineering Company?      A. They are in New York.

Mr. Jones: If the Court please, we have not objected so far, but counsel is going far beyond the scope of the direct examination. I suggest that if he wants to take the witness so far, he should make this witness his own.

Mr. Marcussen: This witness has testified as to the intent of these individuals.

The Court: I think the cross-examination is proper in view of the questioning on direct on intent.

Q. (By Mr. Marcussen): Are you sure that MacDonald Engineering has an office in New York?

A. Yes, sir. They did; I don't know whether they have now.

Q. Do you know whether they have one in Boston?

A. There is a report and it is shown on their stationery. I assume that their head office is up there.

Q. Where else did he take you, Mr. Schnitzer? To what other establishment, if any?

A. I don't remember any except the R.F.C.

(Testimony of Morris Schnitzer.)

Q. Now, did you ask him to take you to MacDonald Brothers? A. No sir.

Q. Was it his suggestion? A. Yes sir.

Q. For what purpose was it? [69]

A. To get an engineering report.

Q. Did you get one? A. Yes.

Q. Do you have it here? A. Not here.

Q. Is it at the steel mill?

A. I don't remember.

Q. Have you supplied one to your attorneys?

A. No, sir.

Q. Do you know whether your attorneys have a copy? A. Of what?

Q. That report?

A. The MacDonald report?

Q. Yes? A. No, sir.

Q. Did Mr. Rosenbaum say anything about what he intended to do with the report?

A. Yes, we did.

Q. What did he say?

A. He would use that to help us in getting an R.F.C. loan.

Q. Was the report submitted, either by you or Mr. Rosenbaum, or anybody else, to Hartley Rogers and Commercial Credit? A. No, sir.

Q. Why not? [70]

A. They did not seem very enthusiastic about the whole thing.

Q. And was the report finally submitted to the R.F.C.? A. Yes.

Q. Where? A. At Portland, sir.

(Testimony of Morris Schnitzer.)

Q. Now, when did you next see Mr. Rosenbaum after you saw him in New York on this occasion?

A. I saw him for a period of two or three months off and on in the period of 1941.

Q. Where in the period of two or three months? Where would you place those visits of Mr. Rosenbaum's in the year?

A. Mr. Rosenbaum came here in July of 1941. He made one trip, as I stated, prior.

Q. That was after your visit to him in New York?

A. Yes.

Q. Now, was there a report sought from any other source?

A. No; the MacDonald report was the only one I had at the time. I had myself made a report previous to this. I had a report previous to the MacDonald report, made by an engineer, Mr. Hunt, of Pittsburgh.

Q. When did you get that report?

A. I am not exact on the date, but I think the first Hunt report was made in the summer of 1941. The MacDonald [71] report, I believe, was finished in the fall of 1941.

Q. Did the MacDonald report contain any recommendations as to the capitalization of this company?

A. I believe that the maximum cost was to be somewhere around \$700,000.00 under that plan, and our maximum capital was to be \$250,000.00 that we would invest.

Q. What did the \$700,000.00 investment represent?

(Testimony of Morris Schnitzer.)

A. We would ask for \$450,000.00 or \$500,000.00 loan at that time, I believe, from the RFC.

Q. By \$250,000.00 capital, was it originally intended to issue all that stock?

A. I don't believe it was, sir, no.

Q. It was not?

A. I think, as I testified a few moments ago, we originally intended to issue \$187,000.00 that we had subscribed for, and hold the balance for Mr. Rosenbaum here and the unissued small balance for either an operator or some other investor.

Q. You suggested on your direct about putting in cash or services which would be the equivalent of cash?      A. That is right.

Q. When you say, or when you said a moment ago that it was originally not intended to issue \$250,000.00, you mean by that, that the Wolf and the Schnitzer families did not intend to take any more than that; is that what you intended [72] to mean?

A. I don't think there was any talk about issuing any more to ourselves.

Mr. Jones: Didn't you misquote yourself?

Mr. Marcussen: I don't know.

Q. (By Mr. Marcussen): Did you speak to the people at the MacDonald Engineering Company, or MacDonald Brothers, or whatever it is?

A. Yes.

Q. And did you tell them of your plan with respect to the limits on the amount of money that



(Testimony of Morris Schnitzer.)

you and your other principals would be able to put into it?      A. That is right.

Q. And did you tell them it was your intention to issue or authorize stock of only \$250,000.00?

A. That is right.

Q. Did they give you an estimate in that report? By the way, will you produce the report?

A. I will have to check to see whether the steel mill has it. There was a copy with the R.F.C.

Q. By the "steel mill," you mean the Oregon Steel?

A. Yes. Now, the R.F.C. should have a copy that went with our original request for our first loan which, by the way, they turned down.

Q. Do you have a copy of it at your office, Mr. Schnitzer? [73]

A. No, sir; I have never had a copy of it.

Q. Have you ever read a copy of it?

A. Yes.

Q. What estimates did they make with respect to the total cost of this plant?

A. I think they were somewheres around \$700,000.00 as a maximum.

Q. I think you testified that as you went along, it got more and more?      A. No, sir.

Q. Didn't you testify there were several surveys after the first survey, and as soon as you got going it appeared that it was going to cost more and more? Didn't you testify to that on direct?

A. A minute ago; I did not on the MacDonald

(Testimony of Morris Schnitzer.)

report. But so far as the plant itself was concerned, as year by year went by, yes.

Q. What other reports were the reports that you referred to? Was that the Hunt report?

A. That was the first report.

Q. What was the occasion for getting the Hunt report?

A. The need for it, first, was to get a plant layout, the type of equipment and the number of men needed.

Q. Wasn't that included in the MacDonald report?

A. The MacDonald report was a separate report on a [74] separate mill layout.

Q. A separate mill of the same company?

A. For the Oregon mill but the production set ups were not the same.

Q. You mean there were differences in these reports? A. Yes.

Q. But they were both submitted in response to the same request for a survey or report?

A. Yes.

Q. What was the occasion for the second report? You had one report with you and you were a little dissatisfied with it? A. How is that?

Q. Were you a little dissatisfied with the first report?

A. No. Very few of the eastern financiers knew Hunt; and in talking with Mr. Rosenbaum he suggested getting MacDonald to make up a regular survey on it.

(Testimony of Morris Schnitzer.)

Q. You did get MacDonald Brothers to get up a report?

A. Yes, I got them second; the original was Mr. Hunt; the second was MacDonald; and the third was Arthur G. McKee Company.

Q. Hunt, MacDonald, and McKee, in that order?

A. Yes.

Q. Can you give me the dates of the requests for reports [75] and the dates of their reports?

A. Not exactly.

Q. As close as you can.

A. The first two were made in 1941, and the McKee request was made in, I believe, 1942; something like that.

Q. Do you have a copy of the McKee report?

A. Yes.

Q. Where is it now?

The Witness: Mr. Jones, have you got that copy with you?

Q. (By Mr. Marcussen): Do you have a copy of the Hunt report?

A. I have some of the copies on that.

Q. Was there more than one report? Was there more than one copy?

A. He made three or four copies of it.

Q. The Hunt report and the MacDonald report were in 1941? A. That's right.

Q. How many weeks or months were there between the two reports; how long an interval?

A. Between the first two?

Q. Yes. A. Two or three, I believe.

(Testimony of Morris Schnitzer.)

Q. Did you ever see the Hunt report?

A. Yes. [76]

Q. Did you show the Hunt report to Mr. Rosenbaum? A. Yes.

Q. What recommendation did that make about capitalization?

A. He had nothing in the first report on capitalization; his was purely a typical mill layout.

Q. Just plans for a mill in the Hunt report?

A. Right.

Q. Was there anything about financing in the Hunt report.

A. Not based on the hourly rate in this area; what he thought it would cost to handle a ton of steel, but nothing on the investment, or anything else like that.

Q. Was that report for the purpose of ascertaining what he thought it would cost to construct the mill, or was it requested for the purpose of ascertaining what the cost of production of such a proposed mill would be? A. No, it was not either.

Q. It was not either?

A. No. I might say that the Hunt report was a sketch of the layout plus how many men it would take at each mill to handle it; and I believe he did on the last page make an estimate of how much it would cost to roll the steel.

Q. And you understand that to be the cost of production? [77] A. Yes.

Q. I am talking about operations, in other words? A. Right.

(Testimony of Morris Schnitzer.)

Q. Do you recall what their estimate was?

A. No, sir, I did not.

Q. Did they request you for any data as to how much stock would be issued?

A. Not in the first report.

Q. Did the first report—that was the Hunt report?

A. Yes.

Q. There was only one Hunt report?

A. That is right.

Q. Do you know how they arrived at the cost of production?

A. Based on the hourly wages which were prevailing in this area.

Q. Do you know whether they took into account any interest on the investment?

A. No, there was nothing about the plant cost or anything else.

Q. Now, what was the occasion for getting the McKee report?

A. The Reconstruction Finance Corporation turned down the MacDonald report completely; they turned down our request for a loan and said that we would have to furnish a [78] recognized steel mill engineer's report.

Q. Did they recommend McKee, or did Rosenbaum recommend McKee?

A. I went out and got the McKee myself.

Q. What was the substance of their report?

A. Well, the report is here, if you want to see it.

Mr. Marcussen: May I see it?

Mr. Jones: It will be offered.



(Testimony of Morris Schnitzer.)

Mr. Marcussen: May I see it in advance of introducing it?

Mr. Jones: Yes.

Q. (By Mr. Marcussen): Did they make any recommendations as to the capitalization of this company? A. No, sir, they did not.

Q. No recommendations about how much stock should be issued? A. No, sir.

Q. Were there any other reports?

A. No, sir.

Q. Did the R.F.C. accept the McKee report?

A. Yes, sir.

Q. And do you know what the estimate was, that is, total cost of the mill and the fixed properties, and the land and fixtures of your enterprise? [79]

A. About one million and fifty thousand dollars; a fraction over one million.

Q. How much did the mill actually cost?

A. The mill actually went up somewhere around \$1,400,000.00.

Q. And when was it completed?

A. Well, that is a hard thing to say when it was completed; I was not there. I had left in July, but I understand that they started rolling steel somewhere around October or November.

Q. I just want to be sure that I understand. This agreement that you referred to between yourself on the one hand and Alaska Junk on the other—check me if I am correct in this feature after I have finished my statement—it was contemplated

(Testimony of Morris Schnitzer.)

that Alaska Junk and you would make advances to Oregon Steel; is that correct?

A. Yes, partly. I would say, "yes."

Q. In what respect is it not correct?

A. At that time too, other advances were larger than mine; their advances were larger than mine. It was past as well as future; they had already advanced a little more than I had.

Q. I am talking about at the beginning. I mean at the beginning when the enterprise started.

A. That guarantee? [80]

Q. You made a guarantee agreement, didn't you?

A. Yes.

Q. Suppose we forget about the guarantee agreement for a moment. I am referring now to a time prior to the guarantee agreement, when you first contemplated the establishment of the mill out there. At that time, was it or was it not contemplated that you and Alaska Junk would make advances to that steel mill?

A. No, that was not contemplated over and above the capital stock that we subscribed for. Of course, there is this that you might say; we had never actually talked about advances while the thing was being formulated.

Q. When did you first have a conversation with representatives of Alaska Junk Company or any of its partners about advances that would be made to Oregon Steel?

A. Well, I think the first conversation that we had, as far as actual advances or for bills to the

(Testimony of Morris Schnitzer.)

steel mill itself, they were those for cash advances for promoting, and so forth; I believe that was about the first charge that they ever made to the steel mill, and I think that came through in 1941—at the end of 1941; I believe it was right around October or November.

Q. Advances were first made by Alaska Junk Company at about that time?

A. Yes, and I think they made a few small ones maybe a [81] month or so prior.

Q. Well, that is shown by this group of accounts which will be definitely offered in evidence as a part of the stipulation which we are going to file here, Mr. Schnitzer. The advances were first made in the month of October, 1941, by Alaska Junk. Now, when did you first make advances; do you recall?

A. My first advance was the expense I had on the thing, which was early in 1941; I think the first expense was the attorney's fees for forming the corporation. I couldn't tell you exactly, but I think it was around the first of June.

Q. Did you include your expenses in your trip to New York, and that sort of thing? A. Yes.

Q. With respect to the advances that were made by you, were all of those advances made for the purpose of organizing the corporation and establishing the steel mill, and so forth? A. Yes.

Q. I think it will be a stipulated fact in this case that Alaska Junk made advances of scrap steel in the amount of approximately \$9,000.00. Now, that scrap steel, I take it, was for the purpose of

(Testimony of Morris Schnitzer.)

operations; is that right?      A. That is right.

Q. That did not go into the plant did it? [82]

A. No, sir.

Q. Did all the other materials or advances, or materials that were purchased in advance, or advances on materials and machinery that were made by you and Alaska Junk—did they go into the plant in general equipment in order to get it established?

A. Not all of that, no sir.

Q. What part did not?

A. We sent down a locomotive crane and some other tools in there which were not actually necessary for the operation. Not that specific equipment.

Q. Did the mill need a crane?

A. It would have needed it later on; when the Alaska Junk decided to send down a little bit of scrape at the start, they had to have a crane there to handle it.

Q. With the exception of the expenses that you had incurred and what might have been incurred on the part of the Alaska Junk, can you tell us whether most of those went into the plant?

A. Most of what?

Q. Was most of the advances made for the purpose of providing funds or materials for the purpose of establishing this organization?

A. I think so, yes.

Q. So far as you know, were there any other materials [83] that were used for operations, that were sent down by either you or the Alaska Junk,



(Testimony of Morris Schnitzer.)

besides the scrap that you have mentioned here in the sum of some \$9,000.00?      A. Yes.

Q. Included in these accounts?

A. I think so; we advanced the money.

Q. What were those items?

A. I could not tell you.

Q. Could you give us generally their classification?

The Court: We will recess until two o'clock this afternoon.

(Whereupon, at 12:30 o'clock p.m., the hearing was recessed to reconvene at 2:00 o'clock p.m., same day, same place.) [84]

Afternoon Session, 2:00 p.m.

The Court: The witness will resume the stand. Whereupon,

MORRIS SCHNITZER

the witness on the stand at the time of the taking of the recess, resumed the stand and testified further as follows:

Cross-Examination

(Continued)

Mr. Jones: If the Court please, before we continue with the cross-examination, I want to say that we have brought into court the formal motions made this morning and the order based on the motion, which reads as follows: "It is ordered that the petitioner may amend her or his petition by adding to the particular paragraph," as I read, and "that the



(Testimony of Morris Schnitzer.)

proposed amended paragraph as set forth in said motion be and the same is hereby accepted as said amendment without the necessity of filing an amended petition." Is that satisfactory, your Honor?

The Court: It is with the Court.

Mr. Jones: The Court asked me if I should bring in the amended petitions, I think I brought in the formal orders substituting the parties.

The Court: Respondent counsel will proceed with the cross-examination.

Q. (By Mr. Marcussen): Mr. Schnitzer, I think we were talking at the conclusion [85] of the session this morning about whether there were any other items advanced by you and Alaska Junk, similar to scrap, which was advanced by Alaska Junk, and I think you stated that there were certain supplies; is that correct? A. That is right.

Q. What were those supplies, if you recall?

A. In addition to the scrap?

Q. Yes?

A. Well, there was some electrical equipment and supplies.

Q. Electrical equipment? A. Yes.

Q. I am talking about any equipment?

A. Spare motors——

Q. I am talking about equipment; I am talking about supplies which would ordinarily be consumed in the operation.

A. Yes; there were extra motors, which are supplies.

(Testimony of Morris Schnitzer.)

Q. What kind of motors?

A. In other words, if a crane has three or four motors, they furnish an extra motor for breakdown purposes; that was done.

Q. Is that the type of thing that you mean by "supplies"?

A. That is right; a lot of it was mechanical; a lot of it was actually raw inventory; and the other was plain supplies. [86]

Q. You stated also that some events occurred to the disadvantage of you and Alaska Junk in connection with the crane that had been supplied?

A. That is true.

Q. What was that?

A. We sent this crane down for temporary use to withdraw the scrap, and the minute it got down there Mr. McGonagle said it was a part of the equipment, and told us to leave it right there.

Q. Was it his contention that it fell under the mortgage with the Reconstruction Finance Corporation?

A. No; it did not actually fall in the mortgage. It would have been used, perhaps, later, or it could have been used. But it was not there for that purpose. It was for temporary use. You must remember this, that practically everything that went in there in the way of equipment, they assumed—the R.F.C.—that they had made their mortgage with that arrangement up there. I will say that in one case or two we got permission to sell one or two pieces of equipment which they found out later we

(Testimony of Morris Schnitzer.)

did not need. The profits would have to go back to the Oregon Steel Rolling Mill.

Q. The entire proceeds? A. The revenues.

Q. With respect to the crane that was supplied by Alaska Junk, was that true?

A. That's right. [87]

Q. Do you know whether that was charged on the so-called open account that you have referred to here, of Alaska Junk?

A. I could not tell you, sir; it is in the record.

Mr. Marcussen: Do you know, Counsel?

Mr. Jones: The accountant informs me that it is.

Q. (By Mr. Marcussen): I think you also stated that it was the intention to issue some stock to Mr. Rosenbaum for his services?

A. That's right.

Q. Were any ever issued? A. No, sir.

Q. Why not?

Mr. Jones: If the Court please, I think that is rather immaterial in this case. We object to it as completely immaterial.

The Court: What about this stock of this corporation? I would like to see who it was issued to. I will overrule the objection.

Q. (By Mr. Marcussen): Can you answer the question?

A. There was some question there as to issuing the stock to Mr. Rosenbaum; Mr. Rosenbaum did not fulfill all the terms of our so-called agreement; in fact, we paid him more money than we were

(Testimony of Morris Schnitzer.)

obligated to under the original [88] agreement.

Q. How much did you pay him?

A. Actually, I think there was \$2500.00 more than the original contract price. There is also a statement in the R.F.C. loan which says that we have not paid any previous money, or will not pay any money to someone else; and that was the reason, on the second loan, we cut it out entirely, on the advice of our counsel.

Q. In what respect had he failed to perform the services that you expected him to perform under the terms of your agreement?

Mr. Jones: The reason I am objecting, your Honor, there is a pending lawsuit in the State Court.

The Court: I don't think that is material.

Mr. Marcussen: I have reason to believe that the answer to that question would be very material. I am willing to make any arrangement whereby the answer to that question could be divulged to me and put into this record without being made public.

The Court: I am permitting counsel to go into the question with reference to this stock, and permitting him a wide latitude; but as to the details, I cannot see how they are material.

Mr. Marcussen: May I ask a specific question?

The Court: Ask any question you like, and I will rule on it. [89]

Q. (By Mr. Marcussen): Was one of the rea-



(Testimony of Morris Schnitzer.)

sons for failing to issue any stock to him for his services, that he failed to produce any capital?

The Court: What is the answer?

A. I beg your pardon, Sir?

The Court: I didn't hear the answer.

The Witness: I did not answer that; I was thinking, sir.

Q. (By Mr. Marcussen): I am referring now to your undertaking when you went down to see the C.I.T. Corporation and to Hartley Rogers.

A. And that, of course, is quite a question to answer at this time. I might say, as to producing capital, actually, and so forth, he did not.

Q. You mean he did not produce it?

A. No, sir.

Q. You have already testified to that, that there was a failure to produce the capital.

A. One of the greatest reasons why the steel mill cost twice as much and cost twice as much in delay and everything else,—

Q. I am not asking you at this time about that. I am asking you now whether one of the reasons no [90] stock was issued for his services was that he failed to produce capital for the organization?

A. It was one of the small items.

Q. It was one of the items? A. Yes.

Q. By "items," I mean reasons; did you understand it that way? A. Yes.

Q. Now, I think you stated that Mr. Wolf particularly had expressed the view that he did not



(Testimony of Morris Schnitzer.)

wish to have the Alaska Junk put any more into this enterprise than approximately \$125,000.00, so far as the capital stock was concerned; is that right?     A. That is right.

Q. Did you have any conversations with the members of the Alaska Junk Company about that limitation which they placed?—which they placed on their contributions of capital stock?

A. Yes, I did.

Q. And what reason was given for that position?

A. Several reasons; one, mainly, that at no time did we ever intend or expect to put in too much money; it was limited by our own capital, in the first place, both I and the Alaska Junk.

Q. And what was the reason why you didn't put in any more capital stock? [91]

A. I had to have something to put in; but I couldn't put in any money when I didn't have it.

Q. Didn't you make substantial advances to the corporation?     A. Yes, I did.

Q. Now, as to the conversations that you had with the Alaska Junk people about this guarantee. When was that guarantee agreement entered into?

A. It was entered into about the same time we re-divided the stock.

Q. When the proportion was changed to one-half for you and one-fourth for each your father and Mr. Wolf, to one-third for you and two-thirds for them; is that right?     A. That's right.

Q. And what was said at the time?

(Testimony of Morris Schnitzer.)

A. It is quite a deal. The thing came up because we saw that I would have to borrow a little cash from the Alaska Junk. Mr. Wolf was very definite that he didn't want to put in too much money.

Q. When you said "I would have to borrow," you meant the Oregon Steel?

A. That is right. Mr. Wolf was very definite then, and it took quite a lot of persuasion to switch the stock around. One of the conditions of the switch was that I would guarantee my one-third end of it. At that time he asked [92] me if I had enough money to take care of my end, and I said I would guarantee one-third.

Q. A while ago you said, on the issuance of capital stock, that Mr. Wolf had said apropos that limitation of Alaska Junk, that he would not put in more than \$125,000.00, and you, presumably, put in one-half of that figure; is that correct?

A. That is correct finally.

Q. Did Mr. Wolf say, or did all of you agree "It is our intention to have this amount only for capital stock"?

A. That is right.

Q. Did you ask about all the other advances that had been made?

A. He knew about them.

Q. He knew about them?

A. Yes, he knew every detail.

Q. Do you recall approximately when that date was that you reduced your interest in the capital

(Testimony of Morris Schnitzer.)

stock to one-third, and when the Alaska Junk interest was increased to two-thirds?

A. I think the meeting was held January 12, 1942.

Q. Well, now, would it refresh your recollection if I would tell you it is going to be a stipulated fact in this case,—

The Court: If it is stipulated, let us not ask about it. [93]

Mr. Marcussen: I was just asking it for the purpose of refreshing his recollection.

The Court: It is immaterial to refresh his recollection if that is the date given. Let us find out if that is the agreement, but let us not try the stipulation.

Mr. Marcussen: I am not.

The Court: Ask him what he said?

Mr. Marcussen: I want to refresh his recollection.

The Court: All right, then tell him just what it is so that you get directly to the point.

Q. (By Mr. Marcussen): It is stipulated that your interest was reduced to one-third of the capital stock on about March 11, 1943.

Mr. Jones: That is when the stock was issued.

Q. (By Mr. Marcussen): So the 1942 date is not correct; it was 1943?

A. That's right; 1943.

Q. Did Mr. Wolf say why he intended that there should be no more capital stock issued?

(Testimony of Morris Schnitzer.)

A. There was never any conversation brought out that there should be any more issued.

Q. I think you testified that there was a conversation at that time,—I think you testified at least in part, with respect to a statement by Mr. Wolf, “That is all we intend to put in, \$125,000.00; that is the extent of our [94] two-thirds interest.” I think you testified similarly to that, and that all you intended was that your one-third should be, namely, \$62,500.00; is that substantially it?

A. Yes.

Q. Did he make any comment why he intended to put in no more?

A. They knew at all times what was being put into the company, and what we had; knowing the Alaska Junk pretty well, I knew they didn’t have too much capital.

Q. Why wasn’t stock taken for some of it?

A. That is why we issued debentures; to take care of some of the loans we had made.

Q. How did you come to arrive at a guarantee agreement between you and Alaska Junk, whereby you would stand the loss, or stand any losses or advances to the extent of one-third and Alaska would stand any losses to the extent of two-thirds of the total advances made by you and Alaska Junk; is that a correct statement of your guarantee?

A. That is about right.

Q. How did you arrive at the figure of one-third and two-thirds?

(Testimony of Morris Schnitzer.)

A. According to the ratio of the stock that was held.

Q. Now, did you ever make any representation to anybody at any time that it was intended that the capital stock of this organization should consist of some \$500,000.00? [95]

A. I don't think so.

Q. Did you ever make any representation to the effect that there might be \$1,000,000.00 of authorized stock, and the amount that would be actually put in and issued would be \$500,000.00?

A. I don't think so.

Q. You are not positive?

A. I am positive, but I would not swear to it.

Q. You would not swear that you ever made any such representation,—that you never made any such representation?

A. No; I would not swear to it.

Q. Did you have a conference with representatives of the press at the time you started this steel mill at all?

A. I don't think I ever met the press; no.

Q. Was it a part of the operation to familiarize the public with the new venture that was going on?

A. There was very little publicity; there was very little of that.

Q. But there was some?

A. The press releases, I think you will note, were made by Senator McNary and the Chamber of



(Testimony of Morris Schnitzer.)

Commerce, with very little said by any of us directly.

Q. Did you see some of the press releases?

A. Yes; I had copies of them.

Q. Would you recognize them? [96]

A. Perhaps.

Q. Do you recall whether there was any statement in any of them that Mr. Morris Schnitzer stated the capital stock would be \$550,000.00,—would be \$250,000.00, and that there would be more capital stock later on? A. No, sir.

Mr. Jones: I object to that unless counsel shows the time, place, and the circumstances under which the statement was given.

The Court: I will overrule the objection.

Q. (By Mr. Marcussen): Mr. Schnitzer, I hand you here a clipping from the Sunday Oregonian of October 5, 1941, and I want to call your attention——

Mr. Jones: Just a minute before you read it into the record.

Q. (By Mr. Marcussen): And I call your attention to the last paragraph of that clipping which purports to quote you.

Mr. Marcussen: Now, does counsel wish to make an objection?

Mr. Jones: Yes, I make an objection to that as incompetent, irrelevant and immaterial; purely hearsay; there is no relationship between the Oregonian, its reporter, its agencies or otherwise and

(Testimony of Morris Schnitzer.)

the steel company that would [97] give counsel the right to use a printed statement as a declaration against interest, unless the witness who wrote the article is produced in court and subjected to cross-examination.

The Court: This is not an attempt to impeach the witness. The question is with relation to the amount of capital stock intended, and I think the purpose is to refresh his memory. I will overrule the objection.

Mr. Jones: May I have an exception?

The Court: Noted.

Q. (By Mr. Marcussen): I call your attention, Mr. Schnitzer, to the last paragraph, which reads "the capital of the corporation originally was listed as \$250,000.00, but this is being expended several times over, Mr. Schnitzer said, the total amount to be announced later."

A. Who was the Mr. Schnitzer?

Q. I call your attention to the fact that that is your name. A. Just let me see this.

Q. Just a minute. Counsel may have an objection. I call your attention to that statement there, and call your attention to the fact that the article opened by a reference to you, in Multnomah County, City of Portland, wherein it said the site of the Oregon Electric Steel Rolling Mills [98] will be established in the Guild's Lake area along the Willamette River, according to Morris Schnitzer, President of the corporation. Isn't that substantially right?

(Testimony of Morris Schnitzer.)

A. That is what the article says.

Q. Did you make that statement?

A. Well, I don't think I ever made the statement.

The Court: That is the question. Did you ever make the statement?

The Witness: I don't think I ever made that statement. One of the reasons I say I didn't make the statement was because at that time in 1941, the corporation was never intended to be a corporation with that amount of capital; nor at any other time.

Q. (By Mr. Marcussen): Now, getting the statement in the newspaper more exactly, didn't you say that if Multnomah County would sell the site, the Oregon Electric Steel Rolling Mills would establish a steel rolling plant in the Guild's Lake area along the Willamette River?

A. Did I make that statement,——

Q. Let me continue. And that the capital of the corporation originally was listed as \$250,000.00, but that amount had been expended several times over, or was being expended?

A. No, I don't think I ever made that statement. [99]

Q. You stated that you saw the small amount of publicity that was going on; did you call the Oregonian up and tell them they had made an error?

A. No.

Q. Did you see this?

(Testimony of Morris Schnitzer.)

A. I couldn't swear whether I actually saw it or did not see it.

Q. But you know you did not call the *Oregonian* or tell them that they had made a mistake?

A. That is right. In fact, if I saw it, I didn't pay any attention to it.

Q. Now, Mr. Schnitzer, I call your attention to a newspaper clipping from the *Oregon Journal*, dated December 3, 1943, and call your attention to the last paragraph of which, reading as follows: "The mill, opened last June,"——

Mr. Jones: Just a minute. Mr. Schnitzer was not in the United States when that was published, and under no circumstances could he be bound.

The Court: The statement contained is not admissible against interest.

Mr. Marcussen: I am asking him if he knows about it.

The Court: Anything that it said?

Mr. Marcussen: I want to refresh his recollection.

The Court: Let him look at it.

Mr. Marcussen: It won't be understood in the record. [100]

The Court: Is there any statement in there purporting to have been made by the witness?

Mr. Marcussen: No; this is a statement concerning the mill of which he was the head.

The Court: Because he was the head, you couldn't bring the newspaper in to use as evidence against him.

(Testimony of Morris Schnitzer.)

Mr. Marcussen: I am simply asking him about it.

The Court: The question is whether he can testify about it. Then, if you ask the question, whether he was responsible for it, that is as far as you can go.

Mr. Marcussen: I submit it is in the nature of an admission.

The Court: The statement in a newspaper is not an admission.

Mr. Marcussen: I am not going to offer it in evidence.

The Court: There is no use asking questions about it if it is not going to be in evidence.

Mr. Marcussen: I am simply asking him if he at any time made a request for additional financing.

The Court: Well, ask the question; you don't have to have a newspaper to ask that question.

Q. (By Mr. Marcussen): Well, I will ask you to read that last paragraph of that clipping, if you will, please (hands paper to witness). [101]

A. I knew nothing about this article here.

Q. I am not asking you whether you knew anything about the article. I am asking you about the sum and substance. Wait until I complete my question.

The Court: Wait until he asks a question before you make a response.

Q. (By Mr. Marcussen): Now, I want to ask



(Testimony of Morris Schnitzer.)

you, Mr. Schnitzer, whether you or anyone else on behalf of the corporation,—you were its president, were you not?      A. That's right.

Q. I will ask you whether you or anyone else on its behalf made an announcement—it refers to an announcement,—      A. Yes.

Q. By the previous owners?

A. What do you want to know?

Q. You were one of the previous owners?

A. Yes.

Q. Did you make the announcement that is attributed to you here, that you were seeking more financing?

A. I never made that statement or indication there.

Q. Or that it was going to close due to lack of finances?

A. Bear in mind that I left here before that statement was made.

Q. No statement of that kind was made by you or with [102] your authority?      A. No, sir.

Q. And you knew nothing about it?

A. No, sir.

Q. Can you account in any way for its appearance in the newspaper, if it were not true?

Mr. Jones: I object to that.

The Court: The question will be stricken. We are not concerned about that, if he doesn't know anything about it.

Q. (By Mr. Marcussen): Do you know whether

(Testimony of Morris Schnitzer.)

your father, pursuant to any power of attorney which you granted him, may have made a statement such as is contained in this article, or in the other article?

A. I am sure he would not.

Q. Are you sure he did not?

A. I am sure.

Q. How are you sure?

Mr. Jones: I object to the question asking him why he is sure, or how he is sure.

The Court: Ask the question about what he knows about it.

Q. (By Mr. Marcussen): Mr. Schnitzer, did you ever make any representation to any bankers that the capital stock authorized would be [103] \$1,000,000.00, and that \$500,000.00 of that amount would be paid in? A. I don't think so.

Q. You never did?

A. I made one statement to the Bank of America that the capital stock would be \$250,000.00; that was made to Mr. Gianinni in 1941, around October or November; sometime in there.

Q. Do you recall whether you made any such representation to officers of the First National Bank of Portland?

A. I don't think I did, sir.

Q. Would you swear that you did not?

A. I would not swear; as I say, I don't remember if I did; and I don't think I did.

Q. You are not certain that you did not?

(Testimony of Morris Schnitzer.)

A. No; I cannot swear to it right now.

Q. Now, in the course of your negotiations with the Reconstruction Finance Corporation, did they make any request of you and the Alaska Junk Company that you put in more capital and put more money into this enterprise?

A. Oh, I don't think they did.

Q. Did you, on behalf of the corporation or on behalf of yourself, ever request a loan at the First National Bank for the purpose of meeting additional capital requirements that the R.F.C. was making? [104]

Mr. Jones: If the Court please, so far as the direct examination was concerned, I didn't go into any of this. I think he has gone far beyond the field or scope of direct examination, and if he wants to question him along this line, he should make the witness his own.

The Court: I don't think so. I think cross-examination should have wide latitude. I will overrule the objection.

Q. (By Mr. Marcussen): What is the answer?

A. Will you repeat the question, please?

Mr. Marcussen: Will you read the question, Mr. Reporter, please?

(Whereupon, the question referred to was read by the reporter as follows: "Did you, on behalf of the corporation or on behalf of yourself, ever request a loan at the First National

(Testimony of Morris Schnitzer.)

Bank for the purpose of meeting additional capital requirements that the R.F.C. was making?")

A. At one time we went to the First National Bank for a joint deal between the R.F.C. and the bank; I believe they were allowed to make a deal of that nature; but the bank wouldn't go for that type of a deal.

Q. [By Mr. Marcussen): And what reason did they give?

A. They said to go to the R.F.C. for the financing. [105]

Q. What reason did they give for not making the loan?

A. I think at that time our capital was not enough; what we intended to put in was not enough.

Q. What you intended to put in was not enough for the bank?

A. They said the maximum capital that we wanted to put in was not enough; that this was strictly an R.F.C. matter, and not theirs.

Q. Had you asked them for a long-term loan?

A. Yes.

Q. And among the reasons that they gave, one was that they didn't make any long-term capital loans?

A. No; the bank could make a long-term loan in participation with the R.F.C.; but they turned us down on this deal.

Q. You stated something to the effect that the

(Testimony of Morris Schnitzer.)

capital stock you intended to put in was not sufficient?

Mr. Jones: He did not state it; that is what the bank stated.

Q. (By Mr. Marcussen): You did not state it, but the bank stated it, I will amend it to conform to Mr. Jones' suggestion. You stated that the bank stated that the capital stock was not sufficient. Is that correct? A. Yes. [106]

Q. What figure did you mention? \$250,000.00?

A. That is right, sir.

Q. Now, some moments ago I asked you a question about why the balance between \$187,000.00 in capital stock issued,—why the difference between that figure and the \$250,000.00? Why wasn't the whole \$250,000.00 issued as originally intended?

A. I answered that question already, on the record.

Q. I want to call your attention to the fact that a part of your answer to that question was to the effect that the R.F.C. would not go for it?

A. No, sir; I didn't answer it that way. It is on the record.

Q. If you did answer it in that way, would that answer be correct? A. I beg your pardon?

Q. If you did answer it in that way, would your answer be correct?

A. Will you repeat the question that you just asked?

Q. Answer if you did make that statement, would that be correct?



(Testimony of Morris Schnitzer.)

A. I did not make the statement.

Q. I am asking you, if you did make that answer to that question in this court, would your testimony be correct, or would it not? [107]

Mr. Jones: I object to what his answer would have been if he had been asked a certain question.

The Court: I will sustain the objection.

Q. (By Mr. Marcussen): The R.F.C. had nothing to do with it then?

A. I beg your pardon?

Q. The R.F.C. did not in any way prohibit you from issuing any more of that stock; is that right?

A. That's right.

Q. Did the R.F.C. make any reference to the issuance of further stock in that connection?

A. No, sir.

Q. Now, in the beginning when you stated that you were going to put in \$250,000.00, or that the capital stock authorized was \$250,000.00, how did you chance upon that figure?

A. The reason I figured it that way, was because in our original estimates, it would come to about \$700,000.00; which was a loan, or intended to be a loan of some \$400,000.00 or \$450,000.00, and \$250,000.00 of our own.

Q. I think you testified that, as time went on, it was apparent you were going to exceed those estimates. Was there any discussion among the stockholders with respect to increased capitalization in accordance with the increased cost of the plant?

(Testimony of Morris Schnitzer.)

A. I think there was once or twice; we tried to get outside people to come in and buy stock, but they would not do it.

Q. Who did you contact?

A. We asked the Dulien Steel Products to come in about the time we formed the corporation, and he turned that down because he was working on a deal himself at that time.

Q. When did you talk to Dulien?

A. I talked to Dulien—I wrote him in April or March of 1941.

Q. And when was the other occasion when an attempt was made to secure additional capital, if any, if you recall?

A. I went to Jack Barde of the Barde Steel Company, and to Sid Woodbury of the Woodbury Steel Company about the same time, in the fall of 1942, with two things in mind, first, to get some capital, and to get them as steel jobbers.

Q. Both of them?

A. Both of them turned the deal down; they were connected with other corporations, for one thing, and would not take a chance; that was the case of Jack Barde. And the other one hemmed and hawed about capital; and neither one of them wanted any stock.

Q. That was about the fall of 1942?

A. That is right.

Q. Why did you try to sell more stock or capital? [109]

(Testimony of Morris Schnitzer.)

A. It was not only a question of getting more capital, but to get more buyers and consumers, and with the added prestige we thought that their names would help us.

Q. Now, it is going to be a stipulated fact in this case that the stock was issued to you, I think, the original stock, some time in 1941; is that correct? A. I think that is correct.

Q. Is that about the time the subscriptions were made? A. That is right.

Q. Were the certificates actually passed to you at that time? Did you receive them then?

A. I think they were kept in the minute book up at Lou Schnitzer's office.

Q. Who was Lou Schnitzer?

A. He drew up the first papers for the corporation.

Q. Can you state what relation he is to you?

A. He is a cousin of mine.

Q. That was sometime in about June of 1941?

A. That is right.

Q. It is also a fact stated in the stipulation which the parties are about to file in this case, that the payment for that stock was made on or about March 31, 1943, I think it is.

Mr. Jones: Just a minute, please.

Mr. Marcussen: Is that about correct? [110]

Mr. Jones: I think it is paragraph 11; I think it is shown in Exhibit 9. I suggest that we stipulate it.

(Testimony of Morris Schnitzer.)

Mr. Marcussen: Well, I want to call his attention to it, and I cannot without identifying it.

Q. (By Mr. Marcussen): Now, it is going to be stipulated in this case that the stock was paid for, as indicated in this Exhibit 9, and it is stipulated, or it will be stipulated as a part of our written stipulation, that Exhibit 9 consists of a transcript of the stock subscription account of Oregon Steel. I direct your attention to the fact that the subscriptions are credited in the amount of \$187,400.00 under date of March 31, 1943; and that that is the time when they were paid. Now, my question is this: can you explain why the stock was subscribed in June of 1941 and was not paid for until March 31, 1943?

A. Well, I think you will find that they were actually paid for.

Q. Well, it is a stipulated fact in this case, or will be when this stipulation is filed—it is included in the stipulation which we have agreed to submit in the course of this proceeding, that payment was made on March 31, 1943; and I call your attention to the fact that that is the date of the entry of a credit of \$187,400.00 to the stock subscription account of Oregon Steel. I ask you if you can explain [111] why the stock was not paid for before that time?

A. The only thing I can think of is this: it was actually voted, and I think it was charged to the Oregon Steel Mills prior to that. I see that this



(Testimony of Morris Schnitzer.)

entry was made at that time; I wasn't even here; I didn't know about it.

Q. You were here in June, 1941?

A. Yes.

Q. And you were President of the Oregon Steel?      A. That is right.

Q. As President, you knew there had been stock subscriptions in the amount of \$187,400.00, as the account shows?      A. That is right.

Q. When did you go into the Service?

A. Actually, I went in in July, 1943.

Q. That is when you went in?      A. Yes.

Q. And from June, 1941, to July, 1943, a period of over two years, during which you had been operating as president of this concern—is that correct?      A. That's right.

Q. Can you give us any explanation as to why it was not paid prior to that time?

A. I beg your pardon; it was paid for prior to that time.

Q. You are not at liberty to state that. I ask that that be stricken, because it is contrary to the stipulation. [112]

The Court: You can ask the question, and, of course, the stipulation will control.

Q. (By Mr. Marcussen): Calling your attention to the fact that we have stipulated to the contrary, do you have any further comments to make?

A. No, sir, I do not.

The Court: We will take a five-minute recess.



(Testimony of Morris Schnitzer.)

(Recess.)

Q. (By Mr. Marcussen): Now, Mr. Schnitzer, I think on your direct examination you testified as to the general nature of the advances that were made by you and Oregon Steel—by you to Oregon Steel—and when I refer to you I include the Schnitzer Steel Products Company; that is your company, isn't it? A. That is right.

Q. I think you testified to the general effect that you both made cash advances; is that correct?

A. That is right.

Q. To a certain extent?

A. That is right.

Q. And you both made advances of materials that were purchased on the order of Oregon Steel?

A. That is right.

Q. Is that correct? [113] A. Right.

Q. And that with respect to purchases which you made, you just made those purchases because you could purchase at a more favorable price than the new corporation; did you state that?

A. No; I did not say a more favorable price. I said that in many cases we bought for them.

Q. Why?

A. In several cases they would not sell to the steel mill, and in several cases, either I or the Alaska Junk bought for them. In some cases some discount was involved, and when we could buy with a discount, we gave them the benefit of it.

Q. With respect to that, you ordered it for them

(Testimony of Morris Schnitzer.)

and it was paid by you, and you paid for it by getting the funds—I beg your pardon—you just charged it up on your respective accounts against Oregon Steel; is that right?

A. That is correct.

Q. Do you have any idea of what proportion of the advances made by you to Oregon Steel consisted of cash advances in this matter?

A. No, I don't. I think the bulk of my advances were of cash, while not exactly to the Oregon Steel, but they were case as I bought equipment for them.

Q. On their order, as you just stated? [114]

A. Yes.

Q. I think you just testified that the third category of advances consisted of items that you sold to them and had in stock; is that correct?

A. That is right.

Q. And the same is true for Alaska Junk?

A. Right.

Q. What did those items consist of?

A. Pipe, steel rails, motors, copper wire; and they also bought a lot of machine work, built three or four rolling tables for the steel mill; and they had a lot of castings made which were charged to the steel mill. I think there were a lot of valves, and fittings, and hose. And they also furnished all of the steel for the buildings. I wouldn't say all of it, but about seventy-five per cent of the steel was purchased from the Tacoma Narrow Bridge, and sent

(Testimony of Morris Schnitzer.)

down to Oakland, California, to be fabricated. They could not get the steel to start with, and that is why we bought the stuff off of the bridge, and the Alaska Junk paid for that. I don't remember exactly how much, but there is a very large array of items in there which both Alaska and I advanced.

Q. On the shipment of these materials?

A. On materials coming in for the mill.

Q. How about the actual machinery of the mill? Was any of that supplied by you and Alaska Junk and charged on these [115] accounts?

A. Well, I bought a lot of steel mill equipment myself; Alaska paid for some of it; and the stuff was all charged to the steel mill.

Q. There were three categories of accounts. Which of the three categories that you have identified here did that machinery fall in?

A. I suppose it would fall in two or three of them; some we bought direct for the mill; others came right out of stock; and on others they advanced stock for; it really fell in all three of them.

Q. A part of the advances were directly cash?

A. Yes.

Q. I think the accounts will show that?

A. They should.

Q. Obviously, when you supplied machinery, that would not be in your cash account?

A. I don't know how they have their books set up.

(Testimony of Morris Schnitzer.)

Q. Did you charge them with the cost of the equipment?      A. That is right.

Q. There was no profit?

A. In fact, I never got a dime for salary or labor for two and one-half years there.

Q. These items that came out of your stock and were sold at the usual profit mark-up, what did they consist of? [116]

A. They consisted of diesel motors, pipe, electric cable conduit. There were hundreds, hundreds of tons of rails that Alaska furnished for the railroad tracks.

Q. That was new equipment?

A. Both new and used.

Q. And how did you determine the price to charge for those items which were forwarded to the corporation?

A. For your information, on second-hand motors, there is a set level that all the motor dealers charge, and that is fifty per cent off the list, or seventy-five; that is what we paid; pipe, the same way; steel, the same way.

Q. In 1941, I think you testified that you went east to New York to see Mr. Rosenbaum, and that you were there in New York for approximately two of the ten days that you were away; and I think you said that you went to Washington and spent considerable time there?

A. That's right.

Q. In connection with finances?

(Testimony of Morris Schnitzer.)

A. That is right.

Q. Whom did you see in Washington?

A. I saw the O.P.M. officials; some of them.

Q. Whom else did you see?

A. That was the bulk of it.

Q. What was the purpose of your conversations with them? [117]

A. To try to get the steel mill okehed.

Q. Did you talk to anyone in Washington about financing in your first week?

A. Not the first week.

Q. Did you go to Washington and talk to anyone there about financing?

A. For about two years, off and on; 1941 and 1942.

Q. In the R.F.C.?           A. That is right.

Q. Who did you talk to there in the R.F.C.?

A. I guess I started at the bottom of the R.F.C. and worked my way up.

Q. Do you recall when the loan was granted or written, when you secured approval—did you get that in Washington, by the way?

A. The word came through the Portland office, I believe. The loans were instituted here, and I think the word on approval was finished here.

Q. Were you given any assurance at any time in Washington that the loan would be granted, in about April of 1942?

A. No, we had no definite assurance that it would be granted; no. I think we got our approval



(Testimony of Morris Schnitzer.)

much later. What was it, somewheres around June or July or August that they approved it.

Q. Well, maybe this will refresh your recollection [118] (hands document to witness). Did you ever send a telegram to Alaska Junk from Baltimore or from Washington in respect to securing approval by the R.F.C. for this loan?

A. Yes, we did; we had a lot of correspondence on this.

Q. Will you read here what purports to be a telegram from the Alaska Junk to you (hands document to witness). Just read it to yourself and see whether it refreshes your recollection.

A. I think I sent this, yes; but I don't think this was the final telegram; I don't think this was the loan that was approved.

Q. Was there ever more than one loan in question?

A. Yes; we had two loans. They turned down the first proposal entirely. That was presented with the MacDonald report.

Q. Only one loan was granted; is that correct?

A. Yes.

Q. And that loan was later increased to \$700,000.00 from \$600,000.00; is that right?

A. That's right.

Q. Having read that telegram, does that refresh your recollection whether you sent that telegram?

A. Yes, I think I sent the telegram.

(Testimony of Morris Schnitzer.)

Mr. Marcussen: If your Honor please, I would like [119] to offer the telegram in evidence.

Mr. Jones: I will object to it as incompetent, irrelevant and immaterial; it does not tend to prove or disprove any of the issues in the case.

Mr. Marcussen: It is all concerned with the financing, if your Honor please.

The Court: I will overrule the objection.

Mr. Jones: May I have an exception, your Honor?

The Court: Noted. It will be admitted as Respondent's number what?

Mr. Marcussen: I am just about to ascertain the number, your Honor.

The Clerk: Respondent's O.

The Court: It will be admitted as Respondent's O.

(The document above-referred to was received in evidence and marked Respondent's Exhibit O.)

Mr. Marcussen: I would like to ask counsel if I might make a copy, and supply a copy of it without removing it from the file.

Mr. Jones: I have no objection.

Mr. Marcussen: We started with the letter "O" for the reason that there are other exhibits attached to the stipulation.

The Court: What is the date of it?

Mr. Marcussen: April 2, 1942, from Morris Schnitzer, [120] this witness, to the Alaska Junk Company.

(Testimony of Morris Schnitzer.)

Q. (By Mr. Marcussen): Mr. Schnitzer, I hand you a copy of the application for a loan, being an application under Section 5-D of the Reconstruction Finance Corporation Act, as amended, consisting of approximately fifteen pages, and I will ask you if that is your signature on the last page (hands document to witness)?

The Court: What date?

Mr. Marcussen: Bearing date of October 29, 1941, if your Honor please.

Q. (By Mr. Marcussen): Is that your signature, Mr. Schnitzer? A. It is.

The Court: What is the answer?

The Witness: It is.

Mr. Marcussen: If your Honor please, I offer this in evidence as a respondent exhibit next in order.

Mr. Jones: We object to this as incompetent, irrelevant and immaterial; it does not go to prove any of the issues in the case in any way and I notice there are some documents attached to it, and I have not had time to examine them. They are dated long after the time when these people had sold their interest in the company. For instance, here is a letter of February 7, 1944. [121]

The Court: I understand all he is offering is the application that was made?

Mr. Jones: It is a part of the application; it seems to be attached to it.

(Testimony of Morris Schnitzer.)

The Court: The only thing I am aware of is the application.

Mr. Jones: May I have a moment to see whether it is made an exhibit to the application?

The Court: Surely.

Mr. Marcussen: I don't think it is, your Honor. May it be understood that these letters which are attached, which have not been signed by the witness, need not be considered?

The Court: The application to the Reconstruction Finance Corporation is material, and I will overrule the objection to that; I will sustain the objection to any extraneous matters.

Mr. Jones: Your Honor, will you save an exception to that?

Mr. Marcussen: I would like to withdraw from the offer any letters contained in this file, which have not been signed by this witness or by the Alaska Junk, or any of its representatives.

The Court: The Court is permitting only the application to be received in evidence, and not the letters. [122] That will be received as Respondent's P, being the application to the R.F.C. for a loan.

(The document above-referred to was received in evidence and marked Respondent's Exhibit No. P.)

Q. (By Mr. Marcussen): Mr. Schnitzer, I think you stated a moment ago that you had made out an application to the Bank of America for a loan in order to finance the Oregon Steel?

(Testimony of Morris Schnitzer.)

A. I made no formal application, no sir; I talked with Mr. Gianinni.

Q. I am referring now to the conversations with Mr. Gianinni?      A. Yes.

Q. What was his response to your conversation about a loan?      A. None.

Q. He did not give you an answer?

A. He was not interested.

Q. Why?

A. He said, "If you want to put more capital into it, then I would make a loan on it."

Q. I call your attention to Exhibit No. E, page 9, which is a part of the application, which purports to be a pro forma statement, and I will ask you to look at that.

The Court: Attached to what application? [123]

Mr. Marcussen: Exhibit P.

The Court: That is the R.F.C. application?

Mr. Marcussen: Yes.

The Witness: Yes, I saw that.

Q. (By Mr. Marcussen): Can you tell me what that is, please?

A. What do you want to know about it?

Q. Can you tell what it is?

A. It is simply a pro forma financial statement estimated as of the date the mill would be completed. This is a tentative estimated financial statement of the mill.

Q. I call your attention to the fact that opposite line 25, under the heading of "net worth" on that



(Testimony of Morris Schnitzer.)

statement—I beg your pardon, opposite line 23, under the heading of “net worth,” the common stock appears with a figure of \$250,000.00; is that right?      A. That’s right.

Q. And that is extended into the margin here and represents the total of net worth as shown by that statement. What did you have in mind in filing that statement with the R.F.C.?

A. That would be the maximum common stock or capital stock issued.

Q. Does it not purport to be a representation of the stock that would be actually issued? [124]

A. “Pro forma” does not mean a definite thing; it is not a formal statement. Don’t forget that this was made out at the time before the mill was complete. You are not talking about actualities; you are talking about future possibilities.

Q. That was your estimate of the capital stock that would be issued?

A. According to this, yes.

Q. That is an estimated balance sheet, is it not, that pro forma statement, as to how the balance sheet of the corporation would look after completion of the mill?

A. Yes, that is an estimated balance sheet at that time. In other words, that is 1941; don’t forget that.

Q. That is correct. And these items listed as assets, they total \$190,000.00, and the total liabilities are in a like figure—I beg your pardon \$890,-

(Testimony of Morris Schnitzer.)

000.00—correction. Can you tell me what those assets are that you have in mind? Are those the assets it was proposed the corporation would have after the completion of the mill?

A. No; that is not true. I think I am right in saying that this financial statement would be the financial statement as the company was ready to operate, or in operating form after completion of the mill. This does not necessarily imply that the raw materials and the cash, and so forth in this plant, shown on this sheet here, are necessary to the [125] finished plant. This is normally over and above the finished plant.

Q. Ready for operation? A. That is right.

Q. And being ready for operation, this item of \$250,000.00 is one of the several items on the liability side, which is balanced against the assets on the assets' side? A. Not all of that.

Q. It is one of the items of the liability side, which enters into the total of \$890,000.00 of liabilities, which offsets assets of \$890,000.00; is that right?

A. If you take it that way; but may I ask you a question.

Q. I think, if you will just answer my questions, and make the answers as complete as necessary, we will get along better. There is no question about are the assets you considered would be necessary to the operation of the mill; is that correct?

A. That is right.

(Testimony of Morris Schnitzer.)

statement—I beg your pardon, opposite line 23, under the heading of “net worth,” the common stock appears with a figure of \$250,000.00; is that right?      A. That’s right.

Q. And that is extended into the margin here and represents the total of net worth as shown by that statement. What did you have in mind in filing that statement with the R.F.C.?

A. That would be the maximum common stock or capital stock issued.

Q. Does it not purport to be a representation of the stock that would be actually issued? [124]

A. “Pro forma” does not mean a definite thing; it is not a formal statement. Don’t forget that this was made out at the time before the mill was complete. You are not talking about actualities; you are talking about future possibilities.

Q. That was your estimate of the capital stock that would be issued?

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Q. It is one of the items of the liability side, which enters into the total of \$890,000.00 of liabilities, which offsets assets of \$890,000.00; is that right?

A. If you take it that way; but may I ask you a question.

Q. I think, if you will just answer my questions, and make the answers as complete as necessary, we will get along better. There is no question about are the assets you considered would be necessary to the operation of the mill; is that correct?

A. That is right.



(Testimony of Morris Schnitzer.)

Q. Now, you stated, I think, that you had made application to the First National Bank of Portland for a loan?      A. That is correct.

Q. And did you testify that that loan had been rejected, or that the request had been rejected?

A. They did not loan the money.

Q. And, among other reasons, it was because they didn't make any long term loans?

The Court: He has already testified about that. Doesn't that speak for itself?

Mr. Marcussen: Yes, I think so.

Q. (By Mr. Marcussen): Now then, from time to time had the mill, as the construction of the mill proceeded, you have already testified that when it was finished it took about \$1,400,000.00; and from time to time did you submit any other pro forma statements to the R.F.C.?

A. No; the R.F.C. man set up a monthly schedule of work to be completed, and so forth, and the amount of money necessary for that work; and that was all. Our accountant is here and he can testify as to that.

Q. Did you have any conversation with the people at the R.F.C. as to what the new pro forma statement would look like in the light of the information that you had any subsequent time to the effect that the mill would cost a little more money than you had originally planned?

A. May I suggest that you ask our accountant that question. I don't think I have any schedule set up or pro forma set up for operations.



(Testimony of Morris Schnitzer.)

Q. Did you ever discuss any pro forma statement with [127] the people at the R.F.C.?

A. I don't think so.

Q. Would you swear to it?

A. No, sir, I would not swear.

Q. After the original application was in, and construction was under way, you do recall, do you, having further conversation with representatives of the R.F.C. as to amounts required, and other details of the financing?

A. We had those right up to the last minute.

Q. I hand you a copy of the document entitled "Certificate of Contributions of Capital," purporting to be signed by you, Morris Schnitzer, President of the Oregon Steel Rolling Mills.

(Hands document to witness.)

The Court: What is the date?

Mr. Marcussen: It is not dated, but makes reference to capital contributions as of November 30, 1942, and bearing also some writings in pen immediately after the signature of Morris Schnitzer.

Q. (By Mr. Marcussen): I will ask you if that is your signature there, and is the penned statement your statement? A. It is.

Mr. Marcussen: I offer that in evidence, if your Honor please, as respondent's exhibit next in order.

Mr. Jones: May I just take a look at it? [128]

Mr. Marcussen: Surely.

Mr. Jones: If your Honor please, it is a case of the partners of the Alaska Junk Company, and not a case in which Mr. Morris Schnitzer is a litigant.

(Testimony of Morris Schnitzer.)

He is not one of the petitioners here, and insofar as this exhibit purports to speak for the Alaska Junk Company, I would have to object to its going into evidence unless counsel shows some agency authority of some kind that would give him the right to make some declaration.

Mr. Marcussen: I direct your Honor's attention to the fact that it contains a statement of the amount of capital contributed by the witness himself, who was the president, and that with respect to the statement as to contributions made by the Alaska Junk, it simply is a statement of the president of the corporation.

The Court: I think it is material. I will overrule the objection.

Mr. Jones: May I ask what this is at the bottom, addressed to Morris?

Mr. Marcussen: I will stipulate that that need not be considered as a part of the exhibit. I think I can clarify it later on, but I am perfectly willing that it be stricken.

The Court: This document will be admitted as Respondent's Q. [129]

(The document above-referred to was received in evidence and marked as Respondent's Exhibit Q.)

Mr. Jones: Your Honor, I realize that you have ruled, but doesn't this show at the bottom that it never went into effect?

(Testimony of Morris Schnitzer.)

The Court: I don't know what it means; I am not considering that at all.

Q. (By Mr. Marcussen): Mr. Schnitzer, I hand you another document bearing title "Agreement Regarding Capital Investment," dated December 29, 1942, executed by Oregon Electric Steel Rolling Mills, by Morris Schnitzer, President, by Schnitzer Steel Products, by Morris Schnitzer, sole owner, and by Alaska Junk, by S. Schnitzer, a general partner, and attested to by H. J. Wolf, and I will ask you if that is your signature at the bottom of the document?

(Hands document to witness.)

A. Yes.

Q. In both instances, for Oregon Steel and for Schnitzer Steel Products? A. Yes.

Q. Is your father's signature at the bottom?

A. Yes.

Q. Is that Mr. Wolf's signature, a petitioner in this case who has recently died?

A. Yes. [130]

Mr. Marcussen: I offer that as the next respondent exhibit in order.

The Court: Is there any objection?

Mr. Jones: No objection.

The Court: It will be admitted in evidence as Respondent's R.

(The document above-referred to was received in evidence and marked Respondent's Exhibit R.)

(Testimony of Morris Schnitzer.)

Mr. Jones: Just to save time in making a new number of this, if counsel does not object, I would like to have the bottom go in (indicating).

Mr. Marcussen: You would like to have the whole thing go in?

Mr. Jones: Yes, subject to my objection to the whole exhibit as to Exhibit Q; that is, the whole exhibit is subject to my original objection.

The Court: I understand you have your original objection.

Q. (By Mr. Marcussen): Mr. Schnitzer, I hand you a copy of another document bearing title "Agreement as to Loans to Oregon Steel by its Stockholders While Mortgage to R.F.C. Outstanding," purporting to be executed on behalf of the Oregon Steel Rolling Mills by Morris Schnitzer, and attested by H. J. Wolf, Secretary. Is that your signature and the signature of Mr. [131] Wolf there (indicating)? A. Yes.

Mr. Marcussen: I offer this as the respondent exhibit next in order.

The Court: Is there any objection?

Mr. Jones: No objection.

The Court: The document just identified will be introduced in evidence and marked as Respondent's Exhibit S.

(The document above-referred to was marked Respondent's Exhibit S and received in evidence.)

(Testimony of Morris Schnitzer.)

Q. (By Mr. Marcussen): Mr. Schnitzer, I hand you another document entitled "Guarantee of Further Capital," purported to be signed by Morris Schnitzer, S. Schnitzer, Rose Schnitzer, H. J. Wolf, Jennie Wolf, Monte L. Wolf, and I will ask you if the first signature there is your signature?

A. Yes.

Q. And is the second signature the signature of your father? A. Yes.

Q. And the third one is of your mother?

A. Yes.

Q. The fourth signature is that of Mr. H. J. Wolf? A. Yes.

Q. And is the next one the signature of Jennie Wolf? [132] A. I think it is.

Q. Do you recognize the last one as that of Monte Wolf? A. Yes.

Mr. Marcussen: I offer that in evidence as the respondent exhibit next in order.

The Court: Is there any objection?

Mr. Jones: I have no objection.

The Court: It will be admitted in evidence, as Respondent's T.

(The document above-referred to was received in evidence and marked Respondent's Exhibit T.)

Q. (By Mr. Marcussen): I hand you another document, Mr. Schnitzer, dated December 1, 1942, which purports to be a letter to the Reconstruction



(Testimony of Morris Schnitzer.)

Finance Corporation, executed on behalf of Alaska Junk, being headed "Re Oregon Electric Steel Rolling Mills," and ask you if you recognize the signature of Sam Schnitzer?      A. I do.

Q. Your father?      A. Yes.

Q. And of H. J. Wolf?      A. Yes.

Mr. Marcussen: I offer this in evidence as the Respondent [133] exhibit next in order.

Mr. Jones: I would like to examine it.

Mr. Marcussen: Surely.

Mr. Jones: I will have to object to it on the ground that it is incompetent, irrelevant and immaterial. Even though it may have stated some sort of an agreement between the Alaska Junk and the R.F.C., it certainly is no evidence as to what the intention was with respect to the account that they actually put in and what they actually regarded as a debt, and what was actually capital. I feel that any contract between two people that may or may not have been carried out is no evidence of intention in this case as to what they were actually investing their money in.

The Court: That was signed by the petitioners in this case, I understand?

Mr. Marcussen: That is right.

Q. (By Mr. Marcussen): Mr. Schnitzer, is your father, Sam Schnitzer, in the courtroom?

A. Yes.

Q. Is your mother, Rose Schnitzer, in the courtroom?      A. Yes.

(Testimony of Morris Schnitzer.)

The Court: I will overrule the objection.

Mr. Jones: Save an exception.

The Court: It will be admitted in evidence and marked [134] as Respondent's U.

(The document above-referred to was received in evidence and marked Respondent's Exhibit U.)

Mr. Marcussen: If your Honor please, I have handed the document to counsel bearing the heading "Certificate," and I wish to offer it in evidence, but before offering it in evidence, I would like to ask counsel whether he has any objection merely because it is a copy, a conformed copy.

Mr. Jones: Have you seen the original?

Mr. Marcussen: I can say this is a copy from the files of the R.F.C. in Portland. I have not seen the originals, because the originals are impounded in the possession of the Federal Reserve Bank of the United States.

Mr. Jones: Subject to corrections for errors on the verification of the original, I have no objection to the fact that it is a copy. Have you got it identified yet?

Mr. Marcussen: No.

The Court: Who is it signed by?

Mr. Marcussen: It is purported to be executed by the Oregon Electric Steel Rolling Mills, by Morris Schnitzer, its president, and attested by H. J. Wolf, whose estate is one of the petitioners in this case.

(Testimony of Morris Schnitzer.)

The Court: What is the date?

Mr. Marcussen: December 29, 1942, and it is not addressed to anyone in particular—yes, it is addressed [135] to the R.F.C. at Portland, Oregon, and it has a statement—if your Honor would like to read it——

The Court: It is a statement about what?

Mr. Marcussen: It is another document made by the corporation in consideration of the loan from the R.F.C. Corporation. Counsel has no objection to it being a conformed copy, and pursuant to our agreement with counsel, it is offered, subject to any correction for any inaccuracies that may be discovered.

Mr. Jones: However, I do have an objection to the exhibit as being inadmissible.

The Court: On what grounds?

Mr. Jones: Not binding on our people; no signature.

The Court: As I understand it, is it agreed that they executed it?

Mr. Marcussen: There is no controversy about that; it was signed by this witness for the Oregon Steel Rolling Mills.

Mr. Jones: If the original is signed, we will waive any objection to the fact that it is typewritten.

The Court: Has the witness said anything about this document?

Mr. Marcussen: If I might be given a moment, I would like to address myself to counsel concern-

(Testimony of Morris Schnitzer.)

ing our understanding as to the admission of the document. May we go [136] off the record?

The Court: Off the record.

(Discussion off the record.)

Mr. Marcussen: I would like to make this statement for the record with respect to counsel's last remark which was contained in the record, addressed to me, that, as I understand it, he has no objection to the introduction of this document in evidence merely on the ground that I have not produced the original, and according to our understanding this may be received in evidence, subject to any corrections which may be made for inaccuracies which may be discovered, and until such a showing is made this document is received in evidence?

Mr. Jones: Without repeating what counsel has said, that merely goes to the identification; that is, to the authenticity of the identification. However, it is not binding on the Alaska Junk Company, it is incompetent, irrelevant and immaterial, and not admissible on that ground.

The Court: There is no objection to the identification, but as to the admissibility?

Mr. Jones: That is right.

The Court: The objection is overruled, and it may be received and marked as Respondent's V.

(The document above-referred to was received in evidence and marked Respondent's Exhibit V.) [137]

(Testimony of Morris Schnitzer.)

Mr. Jones: I want to except to the last ruling.

Mr. Marcussen: I have only a copy of that, and I would like to ask leave to withdraw it. I would like to say also in that regard that I would like to make a general request to withdraw all exhibits for which we have no copies.

The Court: Photostatic copies may be substituted.

Mr. Marcussen: Photostatic copies may be substituted or a return of the original?

The Court: All right.

Mr. Marcussen: If counsel would join in the motion, I would like to make it on behalf of the petitioner as well as myself.

Mr. Jones: That is agreeable.

Mr. Marcussen: If your Honor please, I would like to offer in evidence as Repondent's Exhibit next in order, a paper bearing title "Resolution of Directors of Oregon Electric Steel Rolling Mills," which is signed at the foot of the page by H. J. Wolf.

The Court: Is there any objection?

Mr. Jones: No objection.

The Court: It will be admitted in evidence and marked as Respondent's Exhibit W.

(The document above-referred to was received in evidence and marked Respondent's Exhibit W.) [138]

Q. (By Mr. Marcussen): Mr. Schnitzer, I hand you a copy of Respondent's Exhibit A which is a



(Testimony of Morris Schnitzer.)

part of the stipulation which will be filed in this case——

The Court: What is the date.

Mr. Marcussen: It is entitled "Guarantee," December 15, 1942, and executed by certain individuals, Morris Schnitzer, Sam Schnitzer, Rose Schnitzer, H. J. Wolf and Jennie Wolf; and there is also a copy of a guarantee running in favor of the R.F.C.

Q. (By Mr. Marcussen): I will ask you whether or not any of the loss which you claim was made here pertains to a loss on the guarantee?

A. That is a pretty general question.

Mr. Marcussen: Perhaps counsel will stipulate?

Mr. Jones: Perhaps, if you will give me time to find out what the facts are.

The Court: Perhaps you can do that later on?

Mr. Marcussen: If your Honor please, I would like to call upon counsel to stipulate that none of the bad debt loss they are claiming to be in issue in this proceeding arises in connection with the guarantee made by the individuals that I have just named and identified on Exhibit A, in which they have undertaken to guarantee the repayment of a part or all the principal of the \$700,000.00 loan made by the R.F.C.

Mr. Jones: That is true. [139]

The Court: Does Petitioner's Counsel stipulate the statement of Respondent's counsel is correct?

Mr. Jones: That is correct.

(Testimony of Morris Schnitzer.)

The Court: It is so stipulated.

Q. (By Mr. Marcussen): I hand you Respondent's C, Mr. Schnitzer, which consists of four pages, bearing the heading of "Standby Agreement," executed by Oregon Electric Steel Rolling Mills by Morris Schnitzer, President, and also by Morris Schnitzer, S. Schnitzer, H. J. Wolf and Monte L. Wolf as standby creditors and ask you to take a look at that document and refresh your recollection from it (hands document to witness).

The Court: If it is in the stipulation, what is the sense of having the witness testify to it.

Mr. Marcussen: I am not going to have him testify to it. I am just asking him to identify it for the purpose of refreshing his recollection with respect to some other matter.

The Court: I presume the proper procedure would be to get the stipulation in first. I presume this will be introduced in evidence; it is not in yet.

Mr. Jones: We are going to read it the first thing tonight after we leave, and get it in the first thing in the morning.

Mr. Marcussen: Neither one of us have read it.

Mr. Jones: We have not had time.

The Court: Let us identify the document now, so that the record will be clear.

The Witness: I have not gone over it for years.

The Court: Ask him the questions.

Q. (By Mr. Marcussen): I would like to ask you what conversations you had with representa-

(Testimony of Morris Schnitzer.)

tives of the R.F.C. about the execution of this document, Mr. Schnitzer? Perhaps I could hasten the refreshing of your recollection by summarizing it very briefly, subject to any correction counsel wishes to make, and say,—

Mr. Jones: That document in the stipulation is identified, and we are raising no objection on the ground of authenticity or the veracity of the document, or the fact that it is a photostatic copy; but we do reserve the right to object to certain documents when they are offered.

The Court: That is another reason why the documents should have been in before. He may be questioning about documents that are never received.

Mr. Marcussen: There is no question about it.

The Court: Why can't you ask him about something else?

Mr. Marcussen: I would like to have a moment to confer with counsel.

The Court: Go ahead. [141]

Mr. Marcussen: If your Honor please, I think counsel and I are prepared to stipulate that I may ask questions about the document even though it is not in evidence, and in the event that an objection with respect to the admission of the document is sustained, I will agree that the testimony may be stricken.

The Court: All right. Proceed.

(Testimony of Morris Schnitzer.)

Q. (By Mr. Marcussen): Now, Mr. Schnitzer, I think I can summarize generally this document by saying that it is a document which the R.F.C. and you entered into for the purpose of subordinating any obligations of Oregon Steel through the parties who are signatory here,—subordinating payments of those obligations to the R.F.C.

Mr. Jones: The document speaks for itself.

The Court: What is it that you want to ask the witness?

Mr. Marcussen: I want to ask the witness what the circumstances were,—

The Court: Don't give such a long preamble; it takes too long. That is the reason it takes so long to try these cases.

Q. (By Mr. Marcussen): What were the circumstances surrounding the execution of that document? [142]

A. I think the main circumstances was that the R.F.C. would not advance any money on the loan until they had this signed (indicating document).

Q. To whom did you talk this matter over with?

A. We talked it over with our attorney.

Q. What representative of the R.F.C.?

A. Oh, I believe, Mr. Cruikshank and Mr. Kennedy, their attorneys.

Mr. Jones: That is a written instrument, and all these preliminary things should not be gone into. I object, therefore.

The Court: I think that is a good objection. I



(Testimony of Morris Schnitzer.)

think that is the reason why the law was made. There is no use going into all negotiations which led up to a written document. I will sustain the objection.

Mr. Marcussen: If your Honor please, this is a standby agreement.

The Court: It speaks for itself; you cannot change it by oral testimony; whatever was said or done was merged in the written instrument, and there is no use talking about what each one said before they signed it.

Mr. Marcussen: Very well, your Honor.

Q. (By Mr. Marcussen): In the course of your testimony this morning, you made a statement concerning the reason why the general accounts, [143] which you characterized as open accounts of yours and Alaska Junk Company to Oregon Steel became so high; do you recall your testimony about that?

The Court: Don't go over it again. If he said it this morning, he doesn't have to say it again. Don't repeat.

Q. (By Mr. Marcussen): Do you recall that part of your testimony? A. Yes.

The Court: What did you say?

The Witness: Yes.

The Court: All right. Don't repeat it.

Q. (By Mr. Marcussen): I think you stated that they would have been paid otherwise. Now, what funds were those accounts paid with?

A. I beg your pardon. The question that you asked me is not very well formed?



(Testimony of Morris Schnitzer.)

Q. Do you understand it?

A. Not too well.

Q. I asked you whether you recalled your conversation about why these accounts got so high. Do you recall that you stated that the R.F.C. would not admit them to be paid? A. Yes.

Q. I asked you, if the R.F.C. had permitted them to be paid, what funds were available that would have permitted it?

A. We had a lot of funds up to \$700,000.00; the R.F.C. [144] funds, to pay our bills.

Q. Wasn't it a part of the loan with the R.F.C., that the R.F.C. loan would go in merely for the actual establishment of the plant, and into the payment of new obligations?

A. New obligations?

Q. Yes?

A. Why shouldn't they be paid.

Q. That is not my question.

A. I will answer it then; certainly they should pay some of the obligations that that plant owed us personally.

Q. Did you take it up with the R.F.C.?

A. Yes, definitely.

Q. What did they say?

A. They absolutely refused to pay them at that time; later, however, they paid some of them.

Q. Did you attempt to use the R.F.C. funds to settle those accounts?

(Testimony of Morris Schnitzer.)

A. I don't see how we could have used the R.F.C. funds.

Q. I asked you if you attempted to do so?

A. That is a very poor question; how can I pay myself when the R.F.C. won't let me have that money?

Q. Did the R.F.C. assign a man to see to it that these funds were actually applied to the payment of obligations for plant and equipment? [145]

A. Yes, they did.

Q. And it was the purpose of the R.F.C. that the funds were not to be used for any obligations with respect to such items as had been incurred by you and by Alaska Junk; is that correct?

A. No; that statement is not correct.

Q. In what respect is it wrong?

A. A lot of the funds that we expended were for machinery and equipment for the mill. The R.F.C. did let us have some money for what we expended; they admitted it was a part of the program.

Q. But at one time they placed a man who was in charge of the disbursement of those funds?

A. Yes; they only had one man, Mr. McGonigle.

Q. When did he come on the scene?

A. I think he came on the job just about the time we started to break the ground for the plant. I think he was assigned to us about the first of 1943, or December of 1942; I am not positive.

Q. Was that when ground was first broken for the construction of the plant?

(Testimony of Morris Schnitzer.)

A. No; ground was first broken about October or November of 1942.

Q. And at that time Mr. McGonigle came on the scene, and his approval was necessary for the expenditure of funds [146] for the establishment of the plant; is that right? A. That's right.

Mr. Marcussen: That is all, your Honor.

### Redirect Examination

By Mr. Jones:

Q. When you were talking about this Mr. Brady and Mr. Woodbury, were you going to them to sell steel, or to sell some stock in the corporation? You mentioned that they were connected with corporations. What corporation did you refer to?

A. Mr. Sid Woodbury jobs United States Steel Corporation supplies here in the city of Portland. Jack Barde represents and distributes supplies for, I believe it is, Allan Wood,—for Bethlehem Steel and the United States Corporation.

Q. But it was not the Alaska Junk or the Oregon Steel that you referred to in that connection?

A. No.

Q. That is the point I wanted to clear up.

The Court: You may stand aside.

(Witness excused.)

The Court: Call the next witness.

Mr. Jones: I will call Mr. Manuel Schnitzer.

Whereupon,

MANUEL SCHNITZER

a witness called by and on behalf of the Petitioner, having [147] been first duly sworn, testified as follows:

Direct Examination

By Mr. Jones:

Q. Will you state your name, please?

A. Manuel Schnitzer.

Q. Are you a son of the petitioner herein, Mr. Sam Schnitzer?      A. Yes.

Q. And your mother is Rose Schnitzer?

A. That's right.

Q. Are you now a member of the partnership of the Alaska Junk Company?      A. Yes.

Q. When did you become a partner?

A. 1946.

Q. When did you first work for the Alaska Junk Company?

A. Well, I worked there as a small boy when I was eight or nine years old; over thirty years ago.

Q. When you started there on a full-time basis, when was that?

A. In the fall of 1928.

Q. During the years 1941 and 1942, what were your duties there at the plant?

(Testimony of Manuel Schnitzer.)

A. I had active,—I was active in the management of the company. [148]

Q. Was that also true in 1941?

A. Yes.

Q. And in 1943, did you leave the company for a while?

A. I left in January and went down to the mill on account of the fact that we knew Morris was going into the Army; and I went down there to get acquainted with the operations.

The Court: What year?

The Witness: 1943. That was on account of the fact that we knew that Morris was going into the Army, and I wanted to line things up as best I could, and therefore went down to the mill.

Q. (By Mr. Jones): You took over in the mill when he left for the Army? A. Yes.

Q. Did you continue in that capacity from the time you took over until the sale to Mr. Hall and Mr. Mears? A. Yes.

Q. During the year 1941, and also the year 1942, and that part of January or February of 1943, when you were still at the Alaska Junk Company, what were some of your duties particularly with respect to the pricing of items?

A. Well, I was in charge of pricing and checking.

Q. Who else also did the pricing and checking?

A. Monte Wolf did, also. [149]

Q. Any goods sold by the Alaska Junk Com-



(Testimony of Manuel Schnitzer.)

pany to the Oregon Steel, who would price them?

A. The merchandise was priced by the department heads; for instance, we had six departments: the steel department, pipe department, electrical department, retail store, steel yard, and machine shop. Those departments would price them and I would check to see that the prices were right and the extensions correct.

Q. Before the charges went to the bookkeeper, did they go over your desk? A. Yes.

Q. If you were not there, who checked them?

A. Monte Wolf.

Q. In other words, the checking and pricing of the items which would go into the account, which will be Exhibit 26, I believe,—you are acquainted with that? A. Yes.

Q. All the pricing that went into this account was of material furnished out of your stock and supplied by Alaska to Oregon Steel, and was priced by you or Monte Wolf,—I mean, was it checked by you? A. Checked; that is right.

Q. Are you familiar with this account?

A. Yes.

Q. And the items on it fall into what classes?

A. What do you mean by that?

Q. What are the charges for?

A. For the type of merchandise, you mean?

Q. Merchandise would be one class.

A. The account would be merchandise, cash advances; that is about all.

(Testimony of Manuel Schnitzer.)

Q. I suppose you paid some bills,——

Mr. Marcussen: That is leading.

Q. (By Mr. Jones): Suppose you paid a bill that Oregon Steel had incurred, if that ever happened?

A. Yes, it did.

Q. What would that be?

A. That would be a cash advance.

Q. You would call that a cash advance?

A. Yes.

Q. Now, when you went down to the steel mill, how did you find conditions there?

A. Well, it was quite a turmoil there.

Q. What was the matter?

A. Well, first we had difficulty of getting the materials; promises of equipment to come at a certain date and falling behind.

Mr. Marcussen: Excuse me. The Respondent objects to any questioning along this line on the ground that it is not [151] shown for what purpose it is offered, and it is wholly immaterial what the conditions were at this mill.

Mr. Jones: It is pleaded in our petitions in which the point is raised that the operation bogged down, that they could not make a go of it, and that they became saturated with bills, and I am trying to show that my pleading is true.

The Court: I will overrule the objection.

Q. (By Mr. Jones): Go ahead.

A. The equipment that was promised was months behind; and we had difficulty getting men

(Testimony of Manuel Schnitzer.)

down to the lowest scale of men in the mill for work. For instance, foundry men, and rolling steel-men,—every inch of that mill was fought hard; and it was tough.

Q. Were you there when it was completed and put into operation?      A. Yes.

Q. And when was that?

A. We started the mill and making ingots in June of 1943; but by the end of August was the first time we rolled.

Q. What about the superintendent or the manager there?

A. Well, the superintendent of the mill that we had was Mr. Dawson, an elderly fellow. We had checked up on him and he was supposed to be competent, and he was giving us his promises that the rolls would be finished in two weeks, and when the two weeks would come along he would say another two [152] weeks; and the rolls were necessary for the rolling of the steel; which retarded the operation a great deal.

Mr. Marcussen: I want to reiterate my objection.

The Court: I don't think it is necessary to go into all the details.

Mr. Jones: That was the purpose, to verify the pleading.

The Court: You did not get a good superintendent; and let it go at that.

Q. (By Mr. Jones): Was he able to carry on his functions?      A. Yes.

(Testimony of Manuel Schnitzer.)

Q. Did you get another superintendent?

A. Yes.

The Court: Let us get over that phase as soon as we can.

Q. (By Mr. Jones): Did he do any better?

A. Very little better.

Q. Did you get into production?

A. We were in production, yes.

Q. Did the company make any money while it was in production? A. No.

Q. Now, there is a balance sheet here, that, of course [153] speaks for itself, and I won't talk to you about that. Did you find yourself in any production difficulty?

A. Yes; we could not roll steel properly, fast enough, to make it a practical proposition.

Q. What about your orders?

A. We had a cancellation; we had a large order with the Government, I think it was about a million dollars, which was cancelled.

Q. How about paying people and paying your bills?

A. Well, we could not pay them.

Q. Did you try to get anybody to buy the plant?

A. Yes.

Q. How many people did you approach?

A. Oh, we approached, I would say, ten or fifteen people; whoever we thought would be interested.

Q. Could you just name one or two?

(Testimony of Manuel Schnitzer.)

A. We approached the Bethlehem Steel Company; Republic; United States Steel; Northwest Steel Rolling Mills; Jack Barde of the Barde Steel; Mr. Alexander of the Northwestern Steel Casting.

Q. Did any of them send out any engineers to look it over?      A. Yes.

Q. And did you get as far as negotiations on a price with any of them? [154]      A. Yes.

Q. Who?

A. We negotiated with Kaiser,—a combination of the Edgar Kaiser and the Electric Steel Foundries.

Q. What was the best offer of all that you found?

A. The best offer was the one that we got from Mr. Hall and Mr. Mears.

Q. Why did you sell it?

A. We had to sell it; we couldn't do anything about it.

Q. How was the sale handled? Did you sell the properties or the capital stock?

A. We sold the capital stock; we sold the debentures.

Q. I believe that is all in the stipulation, and we won't go into that. You say the mill was fought out hard every step of the way. What do you mean by that?

A. Well, we had difficulties with the men; first of all, with the personnel for operating the mill. The management,—the manager tried,—we tried to



(Testimony of Manuel Schnitzer.)

get proper managers; we did everything in the world to get good men and just couldn't get them. We called back east to Arthur McKee, the famous national engineer for steel mills, and we just could not get him to recommend anybody for us; men were not available.

Q. Did anything happen to you while you were on the job?

A. I developed stomach trouble and got sick.

Q. While you were working there?

A. That's right. [155]

Q. What was the cause of that?

Mr. Marcussen: The Respondent objects to that.

The Court: Sustained.

Q. (By Mr. Jones): How many hours a day did you put in down there?

The Court: I will overrule the objection. Answer the question.

A. We worked ten or twelve hours a day.

Q. (By Mr. Jones): How were things going so far as your plans were concerned; were they working out? A. No.

Q. Did you meet any objection from other steel companies operating in this area?

A. Very much.

Q. How, and of what nature?

A. We had a basic order,——

Mr. Marcussen: I will object to that.

The Court: I will overrule the objection. Go ahead.

(Testimony of Manuel Schnitzer.)

A. (Continuing): The Pacific Chain Company in town were making anchor chains for the United States Maritime Commission, and their basic order which they promised us when we were building the mill would have carried the overhead of the mill; we had rolled several thousand tons of [156] steel for them, and we could have handled the order, but when we had the steel rolled, on a certain order, and we asked for a future order, as they had promised, they said they would be unable to do it because Bethlehem Steel were refusing to give them other sizes that they were buying from them; and they just could not give us any hope at all.

Q. How did the Alaska Junk Company obtain the money with which they made advances for and on behalf of the Oregon Steel?

A. We had some money of our own; some of it was merchandise that we sold, and a large percentage was borrowed from the bank.

Q. On what kind of terms?

A. Ninety days.

Q. On ninety-day bank loans?

A. That is right.

Q. With respect to the Alaska Junk Company's own cash position, what would have been the result had they put more money into it than \$125,000.00?

Mr. Marcussen: Just a moment. May I have that question read?

(Testimony of Manuel Schnitzer.)

(Whereupon, the last question was read by the reporter as above recorded.)

Mr. Marcussen: I'll object to that as calling for a conclusion of the witness. [157]

Q. (By Mr. Jones): You were the manager at the time? A. Yes.

Q. Do you know what the effect would have been on Alaska if they had put more money into it?

A. Our accountants advised me that that was the maximum that we could afford to put into the company.

The Court: Who advised you?

The Witness: Our accountants.

Mr. Marcussen: May I have that identified as to amount and date?

Q. (By Mr. Jones): When was that?

A. Well, I discussed our company financial affairs with our accountants quite often, as I depended upon them for our technical advice; but I wouldn't know exactly what date that happened; but we always planned in advance, and it was very definite that that was the advice that they gave me.

Mr. Marcussen: With respect to the stock of \$187,000.00?

Mr. Jones: May I make the suggestion that you cross-examine when the time comes.

Mr. Marcussen: Then may I have it ascertained what amount you are talking about; I think I am certainly entitled to that. [158]

The Court: Make the question more definite.

(Testimony of Manuel Schnitzer.)

Q. (By Mr. Jones): Do you know what time you are talking about? A. 1942.

Mr. Marcussen: Now, in excess of what amount?

The Witness: In excess of \$125,000.00.

Q. (By Mr. Jones): That was the amount that you first mentioned, wasn't it?

A. That is right.

Q. And do you know anything about a guarantee that existed between the Alaska Junk Company and Mr. Morris Schnitzer? A. Yes.

Q. How did you gain knowledge of that?

A. It took place at my mother's house.

Q. Did you ever hear anything about it in the course of your business or not?

A. Yes, I did.

Q. Do you know whether there were any entries on the books of Alaska Junk about it?

A. Well, we had a guarantee at the end,—after we sold the mill,—we had made a guarantee,—I mean, Morris had \$83,000.00 worth of second mortgage which he turned over to the Alaska Junk on account of the guarantee. [159]

Q. I know, but when was the guarantee made?

A. 1942.

Q. About what month in 1942?

A. I believe it was December.

Q. Before you sold the mill stock to Mr. Hall and Mr. Mears had any efforts been made that you know of to sell any of the unissued stock or to procure more money with which to carry on?

(Testimony of Manuel Schnitzer.)

A. We had tried to interest the capital.

The Court: I didn't hear you.

The Witness: We had tried to interest capital.

Q. (By Mr. Jones): Did you have any success at that?      A. No, sir.

Q. Now, the reasons for your sale, were they all these various factors that you have enumerated?

A. Yes.

Q. Do you know anything about the,—do you personally know anything about the transaction that resulted in the Alaska Junk Company raising its stock interest or taking more stock than the original amount of 625 shares that the partners had, up to 1250 shares?

A. Morris had subscribed to 1251 shares, and he saw that he could not fulfill that subscription. He took it up with Mrs. Wolf and Mr. Wolf, and my dad and my mother, and [160] they had to take an extra 625 shares of his; but Mr. Wolf made him promise or guarantee that, if there was any loss if he did not come up to his one-third, he would make it good.

Q. What I am particularly inquiring about is whether you overheard any conversation or whether it came to you in any way officially?

A. I was in my mother's house when it happened.

Q. Did you ever hear any statement about how much money the Alaska would put into the rolling mill?



(Testimony of Manuel Schnitzer.)

A. Mr. Wolf always maintained that he would not put in any more than \$125,000.00.

Q. When you say Mr. Wolf, do you mean Mr. Wolf on behalf of himself, or on behalf of the Alaska Junk?

Mr. Marcussen: I'll object to that.

The Court: Sustained.

Q. (By Mr. Jones): In the course of the conversation, who was Mr. Wolf talking about, the investment of Alaska Junk, the investment of himself personally, or just who was he talking about?

A. Being that Mr. Wolf was a partner, it wouldn't make any difference; it was for himself or the Alaska Junk.

Q. My question is, do you know what amount the Alaska Junk Company partners, the partnership itself, all of them—put as a limit of investment of capital in the Oregon Steel? [161]

A. They agreed not to put in over \$125,000.00.

Q. A little while ago when you remarked about what Mr. Wolf said would be the limit that could be put in, was the contribution that he was speaking about on behalf of Alaska or on behalf of himself?

A. You understand, Mr. Wolf figured that it was one-half of the 1250 shares which the Alaska Junk Company had at that time; that was one-third of the subscribed stock; and he realized that with Morris Schnitzer having 625 shares, approximately, and Sam Schnitzer with 625 shares, that would be

(Testimony of Manuel Schnitzer.)

a control of the stock; and for that reason he did not want to go too strong.

Q. I realize that, but what I am trying to find out is what was the conversation when he mentioned the \$125,000.00 concerned with; was it concerned with what the Wolf would put personally into the business, or what the partnership would put in there?

A. I don't understand the question.

Mr. Marcussen: I object to the question on the ground that it is not the best evidence, anyway; this man's father is in the courtroom.

The Court: He was not a member of the partnership?

Mr. Jones: He was manager of the partnership.

Mr. Marcussen: And his father, a member of the partnership, is in the courtroom. [162]

Q. (By Mr. Jones): Had the Alaska Junk Company ever promoted and financed any other businesses besides this? A. Many of them.

Mr. Marcussen: I will object to that and ask that the answer be stricken. It calls for a conclusion as to whether or not he promoted any other concerns.

The Court: I think that is a fact rather than a conclusion; I will overrule the objection.

Q. (By Mr. Jones): Would you state the names of some of them?

A. The Alaska Junk formulated the National Machinery Company in Eugene; the Industrial Air

(Testimony of Manuel Schnitzer.)

Products of Portland; the Central Supply Company of Portland; the Carlton Coast Railroad Liquidators; oh, gosh, that was our general practice; we did it for years.

Q. The companies that you did not yourself organize or have stock in, did you ever furnish any financing to any of them?           A. Yes.

Q. Will you name some?

A. Hesse-Ursted Company.

Q. What business were they engaged in?

A. They are a machine shop.

Q. What about dealers in scrap metal? [163]

A. It was a general practice all the time to advance money to dealers, to any industry where we saw a chance to make a profit by helping them and by buying or selling them materials.

Q. What was the motive of making these loans and organizing these companies?

A. For instance, Hesse-Ursted were in bad financial straits; we loaned money to them; they were in difficulties.

Q. How much of a loan was that?

A. It was approximately \$50,000.00.

Mr. Marcussen: When?

The Witness: In 1941. As a result of that loan we got a customer and they got all their cast iron from us, and any of the merchandise that we could supply them with.

Q. (By Mr. Jones): Was the purpose of these

(Testimony of Manuel Schnitzer.)

loans to finance and credit companies and sources of supply?

Mr. Marcussen: I will object to that as a leading question; this is in the nature of a cross-examination.

The Court: I will overrule the objection.

Mr. Marcussen: He is putting the words in the mouth of the witness.

Q. (By Mr. Jones): Go ahead and say what was the purpose?

A. The purpose was either to sell the men merchandise [164] so that we would have an edge or advantage, so that we could profit, naturally; in order to buy or sell to or from them.

Q. These debentures that were taken by the partners of Alaska Junk from Oregon Steel,—was anything ever received on them prior to the time that they got the second mortgage?

A. From the new owners?

Q. From the new owners? A. No, sir.

Q. Now, what sort of a cash account, money in the bank, cash, petty cash, and so forth, did Alaska Junk Company ordinarily maintain?

A. Our balance was generally small.

Q. By "small," what do you mean?

A. Approximately five to ten thousand dollars.

Q. Was there any time in the month that you would have a high balance?

A. It would be possibly around the tenth of the month; often we were overdrawn.

(Testimony of Manuel Schnitzer.)

Q. Do you know what was anticipated as to the probable earnings of the Oregon Electric Steel when Alaska Junk put its money in there?

Mr. Marcussen: I'll object to that; no foundation laid; it calls for a conclusion of the witness.

The Court: That is the manager of the company? [165]

Mr. Marcussen: He is not manager?

Mr. Jones: He was manager of the Oregon later.

Mr. Marcussen: He was manager of the Oregon Steel after Morris Schnitzer left.

The Court: After the loan was made?

Mr. Marcussen: After the loan was made and the entire corporation was set up.

The Court: I will sustain the objection.

Q. (By Mr. Jones): Now, as one of the managers of the Alaska Junk, and in the course of your work and duties there did you hear or did it ever come to you in your business, as to what the Alaska Junk expected to receive from the Oregon Steel in the way of credit extended, or because of credit extended?

Mr. Marcussen: I'll object to that.

The Court: I think it would be hearsay; I sustain the objection. It would be decidedly self-serving.

Q. (By Mr. Jones): Now, then, the balance sheet in evidence of the Oregon Steel, that is of October 31, 1943, and the sale was on November 26, 1943. Do you know whether there was any substantial activity from the first of November to the 26th of November?           A. Very little.



(Testimony of Manuel Schnitzer.)

Q. Were you making steel during that time?

A. No; we were down.

Q. You were down? A. Yes.

Q. Did the debit and the credit, and the asset and liability picture change from that shown in the document?

A. No; we had a very small crew there; there was nothing done.

Q. Now, the liabilities shown on that balance sheet as of October 31, 1943, what can you say with respect to any change in that on November 26th?

A. I don't understand your question.

Q. Was there any substantial change in the liability picture between the 1st and the 26th of November? A. Not much.

Q. Are you acquainted with the activities of your father and Mr. Wolf in the Alaska Junk Company during the years 1941, 1942 and 1943, both concerning the duties that they performed and the time that they spent there? A. Yes.

Q. Were there any substantial changes in what they did? A. In those years?

Mr. Marcussen: I'll object to that, if your Honor please, on the ground that it is not the best evidence; this witness is not one of the partners.

The Court: I will overrule the objection. Proceed. [167]

A. No, sir.

Q. (By Mr. Jones): Now, then, do you know whether the activities, interests, and so forth of your

(Testimony of Manuel Schnitzer.)

mother and of Mrs. Wolf were any different in 1942 and 1943 than they were in 1941?

A. No, sir.

Q. Will you tell us when you were born?

A. 1907.

Q. And where did the family live?

A. We lived on Fifth and Jackson Street.

Q. From what years?

A. What years we lived at Fifth and Jackson?

Q. Yes?

A. We lived there from approximately 1917 to 1934.

Q. Where did you live after 1934?

A. We moved up to Vista Street.

Q. And do they still live there?

A. Yes, they stil live there.

Q. When did you marry and leave the family home?      A. 1936.

Q. Now, during the years after you were old enough to remember, in these two places where you lived, do you remember whether or not Mr. and Mrs. Wolf ever came over to your house?

A. They were there practically every night of the week. [168]

Q. And do you have any independent and personal recollection of any of the topics of conversation?

A. The usual topics of conversation were the business.

Q. Well, can you recall any specific topic or subject that was talked about?

(Testimony of Manuel Schnitzer.)

A. We used to discuss the steel mill,—generally the main discussions were business.

Mr. Marcussen: When you were a small boy?

Mr. Jones: I will straighten the times out, counsel. I am as interested as you are in getting this over with.

A. They would discuss the things at night; the general business of the day.

The Court: Who do you mean by “they”?

The Witness: Mr. and Mrs. Wolf and my dad and my mother.

Q. (By Mr. Jones): And during the working hours down at the Alaska Junk Company, were there many discussions between your father and Mr. Wolf,—

Mr. Marcussen: May this be identified as to time. I have asked that on several occasions.

Mr. Jones: I am coming to the time.

Mr. Marcussen: We ought to know at the time you are asking the questions.

The Court: Give the time. [169]

Q. (By Mr. Jones): Now, then, down at the Alaska Junk Company during the years 1941 and 1942 and 1943, were there many discussions between your father and Mr. Wolf on matters of business policy and things of that kind?

A. Yes.

Q. Prior to those years, where did they hold their business discussions?

A. They were mostly held at home, at our house.

(Testimony of Manuel Schnitzer.)

Q. Now, when such things as the organization of the Central Supply Company that you mentioned,—

Mr. Marcussen: I will object to the question on the ground that it is leading; there is nothing in the evidence about it yet.

Mr. Jones: He mentioned the Central Supply.

Mr. Marcussen: He simply mentioned the Central Supply as one of the organizations to which loans were made by the Alaska Junk. He did not say the Alaska Junk organized it.

The Court: Will the reporter read the question?

(Whereupon, the last question was read by the reporter as above recorded.)

Mr. Jones: I was trying to make it short, but if I have to do it the long way, of course, I will.

The Court: Ask the question. [170]

Q. (By Mr. Jones): Did you organize the Central Supply? A. Who do you mean?

Q. Who organized the Central Supply?

A. The Central Supply was organized by Sam Schnitzer, Rose Schnitzer, H. J. Wolf and Jennie Wolf.

Q. When was it organized?

A. The Central Supply was organized approximately in 1939.

Q. During the months before they organized the company, did you ever hear any conversations at that time concerning it? A. Yes.

Q. When was Industrial Air Products organized? A. That was organized in 1939.

(Testimony of Manuel Schnitzer.)

Q. Who by?

A. By Morris Schnitzer, Sam Schnitzer, Rose Schnitzer, H. J. and Jennie Wolf.

Q. Were there any conversations about different organizations prior to that time? A. Yes.

Q. Particularly about the organization of the Industrial Air? A. Yes.

Q. Where were they held? [171]

A. They were held at home.

Q. Who participated in that?

A. All of the parties; the five parties.

Q. Who were they?

A. Rose Schnitzer, Sam Schnitzer, H. J. Wolf and Jennie Wolf, and Morris Schnitzer.

Q. Were they the parties who participated in the organization of the Central Supply?

A. Yes.

Q. Do you know, of your own information, when the decisions were made to go ahead and organize those companies?

A. Which company are you referring to?

Q. Let us take Industrial Air.

A. Industrial Air?

Q. Yes.

A. We decided in about January of 1936 to organize that company.

Q. Where was the decision made?

A. It was made at my mother's house.

Q. And who was present at the time of the decision?



(Testimony of Manuel Schnitzer.)

A. Morris Schnitzer, H. J. Wolf, Jennie Wolf, Sam Schnitzer and Rose Schnitzer.

The Court: What kind of a company was it?

The Witness: Industrial Air manufactured oxygen and acetylene, and the selling of it. [172]

Q. (By Mr. Jones): Does Alaska Junk make purchases of Industrial Air? A. Yes.

Q. Does it sell to Industrial Air? A. Yes.

Q. Has Alaska Junk ever advanced cash to them? A. Yes.

Q. Now, with respect to Central Supply, where was the decision made with respect to the final entering into that deal, that is, that they would go ahead and organize it?

A. At the Sam Schnitzer residence.

The Court: What business was Central Supply in?

The Witness: Wholesale plumbing and electrical goods.

Q. (By Mr. Jones): Were there any business relations between Alaska Junk and the Central Supply? A. Yes.

Q. What were they?

A. We buy from them, and sell to them.

Q. Did Alaska Junk ever make cash advances to them? A. Yes.

Q. Do you have any personal knowledge of the organization of the National Machinery Company?

A. I believe the ownership was in Sam Schnitzer, Rose [173] Schnitzer, H. J. and Jennie Wolf.

(Testimony of Manuel Schnitzer.)

Q. And did you know about it when it was organized?      A. Yes, I did.

Q. When was it?

A. Approximately 1927.

Q. How old would you have been at the time it was organized?

A. I was going to college; I was about nineteen.

Q. Where did you go to college?

A. I went to Reed College and the University of Oregon.

Q. Were you going to college at the time it was organized?      A. Yes.

Q. Where?      A. Reed College.

Q. Were you living at home?      A. Yes.

Q. Did you ever hear any discussions about the organization?      A. Yes.

Q. Where were those discussions?

A. They were made at home.

Q. Who participated in them?

A. Mrs. Rose Schnitzer, Sam Schnitzer, Jennie and H. J. Wolf. [174]

Q. Do you know when they finally came to a decision to organize that company? Where it was made?      A. At home.

Q. Who were there at the time?

A. H. J. Wolf, Jennie Wolf, Sam Schnitzer and Rose.

Q. And did they all participate in the discussion?      A. Yes.

Q. Did the Alaska Junk Company have any busi-

(Testimony of Manuel Schnitzer.)

ness relation with the National Machinery Company?      A. Yes.

Q. What?

A. We sold them a tremendous amount of merchandise.

Q. Did you ever supply them any cash?

A. Yes.

Q. Now, what is the Carlton and Coast Railroad Liquidators, which you mentioned?

A. That was a company that the Alaska Junk Company and the Dulien Steel Products of Seattle organized for the purchase and dismantling of the Carlton Coast and the Flora Logging Company Railroad.

\* \* \*

### Direct Examination

(Continued)

By Mr. Jones:

Q. Last night we were discussing companies that were organized or financed by the Alaska Junk Company. You named certain companies that were organized by the Alaska Junk and financed. I think the last one we discussed was the Carlton and Coast Liquidators. Were there any others?

A. Yes, the Vaughan Motor Works; the Steel Tank and Pipe Company; also we had Sam Choat at Marshfield.

Q. What was the name of his business?

A. It was the Coos Bay Salvage Company, and he changed it over to "Industrial Steel and Supply."

(Testimony of Manuel Schnitzer.)

Q. What was the Marshfield Bargain House?

A. The Marshfield Bargain House was another company.

Q. Were any advances made to it?

A. Yes.

Q. What about M. Turn?

A. What do you want to know about him? [187]

Q. Who was M. Turn?

A. He was a dealer up in Pendleton; he dealt in scrap and usable materials.

Q. Did the Alaska Junk advance him any money?

A. We advanced him considerable amounts from time to time.

Q. What was the firm of Munce and Pedrante?

A. They were a couple of men that dealt in scrap metals and had trucks and did hauling.

Q. Were any funds advanced to them?

A. Yes.

Q. Who was Emil Nyberg?

A. He was a man that operated on dismantling railroads and scrap materials.

Q. Who was R. Pedrante?

A. That was Munce and Pedrante, and later they were split up and were working as individuals.

Q. Is that the same as Munce and Pedrante?

A. It is the same Pedrante.

Q. What did he do?

A. He had trucks, and would dismantle mills and

(Testimony of Manuel Schnitzer.)

logging camps, and he did a similar type of work.

Q. What was the Medford Bargain House?

A. It was a company in Medford we bought scrap iron from. [188]

Q. Did you ever make any advances to them?

A. Yes.

Q. Now, over what period of years did those advances occur that we have discussed, beginning with the Marshfield Bargain House, and all that I have mentioned in between?

A. I would say between 1930 and 1945.

Q. Last night before we closed, I had asked for a document which I would like to have marked as Petitioner's 28.

(The document above-referred to was marked for identification as Petitioner's Exhibit No. 28.)

Q. (By Mr. Jones): I am handing you Petitioner's 28, and I will ask you, after counsel sees it, if you signed it, and to state what it is.

A. This is an agreement of joint venture between Sam Schnitzer, Harry J. Wolf, Jennie Wolf, Rose Schnitzer, with the Dulien Steel Company in the Carlton Coast venture.

Q. What was the Carlton Coast venture?

A. The Carlton Coast venture was a joint venture made up by the joint partners and the Dulien Steel for the purpose of dismantling and sale of the Carlton Coast Railroad and the Flora Logging Company.



(Testimony of Manuel Schnitzer.)

Mr. Jones: I offer that in evidence as Petitioner's 28. [189]

Mr. Marcussen: The Respondent objects to that, if your Honor please, on the ground that it has nothing to do with the issues in this case. It is simply a partnership agreement entered into between certain principals, Sam Schnitzer, Harry Wolf, Rose Schnitzer and Jennie Wolf, with another corporation in Washington. I don't see that it has any materiality.

Mr. Jones: One of the things that I must establish is that we were in the habit of financing, and promoting other business enterprises; and that is one of the enterprises that the Alaska Junk Company financed; it is evidence of the scale of operations that that company financed.

Mr. Marcussen: There is no mention in the document of Alaska Junk Company; it is merely an indication that certain individuals entered into another business.

The Court: The individuals are the petitioners here?

Mr. Marcussen: Yes, your Honor.

The Court: I think with respect to whether or not the advances were made in the nature of capital investments or loans, that might shed some light on the activities of the parties contemporaneously or over a period of time.

Mr. Marcussen: Before your Honor rules, I would like to ask a question.

(Testimony of Manuel Schnitzer.)

The Court: All right. [190]

Mr. Marcussen: Is there any evidence here of financing made to anybody (refers to document)?

Mr. Jones: The document speaks for itself.

Mr. Marcussen: I am asking him on voir dire whether there are any.

The Witness: What is the question?

Mr. Marcussen: Is there any reference anywhere here to any advances?

The Witness: Yes.

Mr. Marcussen: Will you point it out, please?

The Witness: Right here (indicating). Shall I read it?

Mr. Marcussen: Don't read it out loud. I am talking about advances which parties of the first part made to any other party, or anybody else named in the document?

The Witness: What do you mean by that?

The Court: Let the Court see the document.

Mr. Marcussen: Yes, your Honor (hands document to the Court). There is no mention in this document about advances made to anybody.

The Court: Just let the Court see it.

Mr. Marcussen: Surely. The Respondent submits that that document has no more bearing on this case than if he were to show that these parties invested in bank stock, for example, or bought real estate. [191]

Mr. Jones: I will develop a few more questions on this, if that is what you want.

(Testimony of Manuel Schnitzer.)

The Court: All right. Go ahead and ask the other questions.

Q. (By Mr. Jones): What was the Carlton Coast Liquidator operation?

A. The partners of Alaska Junk purchased a portion of the Carlton Railroad from the R.F.C., and the Dulian Steel Products purchased the back end of that railroad from the Bank of California. We joined together, due to the fact it was one railroad, but had several ownerships of several properties; we joined together in dismantling and selling this logging railroad.

Q. Were a separate set of books kept for the Carlton Coast Liquidators? A. Yes.

Q. Completely separate from the Alaska Junk Company? A. Yes.

Q. Did the Alaska Junk Company keep an account on its books with the Carlton Coast?

A. Yes, they had an account on their books.

Q. Showing credits and debits which passed back and forth between the two entities?

A. Yes.

Q. Is this document, Petitioner's 28, the document [192] which creates the joint venture between Dulien Steel and the Alaska Junk Company?

A. Yes.

Mr. Marcussen: I'll object to that. There is no mention in that of the Alaska Junk Company; and

(Testimony of Manuel Schnitzer.)

the question calls for a conclusion of the witness; and I ask that the answer be stricken.

Mr. Jones: Very well.

Q. (By Mr. Jones): How have the Carlton Coast Liquidators been treated on the books of the Alaska Junk Company?

A. It has been treated as a separate company.

Q. And the Alaska Junk has an account with it?

A. Yes.

Q. Has Alaska ever made advances to it?

A. Yes.

Q. Were they substantial? A. Yes.

Q. Do the partners of the Alaska Junk Company who are mentioned in this document, Petitioner's 28,—do they maintain any other set of books of their accounts with the company, other than the books that Alaska maintains?

A. No, sir.

The Court: This contract deals with two individuals, in the case which compose the Alaska Junk Company, and this [193] contract is entered into between those parties and this other concern on April 20, 1941, which is within a couple of years or within a year and a half of the time involved. I don't know just what probative force it might have, but I think the Petitioner might have it considered as a part of the system of petitioners' methods of doing business with reference to financing other corporations and other parties for use in their own business. That is about what the effect of it is.



(Testimony of Manuel Schnitzer.)

It might be an investment, as Respondent contends, but I think, in view of the issues involved here, I will allow the evidence and overrule the objection.

(The document heretofore marked Petitioner's Exhibit No. 28 for identification, received in evidence.)

Mr. Marcussen: Exception.

Q. (By Mr. Jones): Is this venture still in operation, or has it been closed?

A. It is still open.

Q. You are still advancing credits to it?

A. Yes.

Q. I want to go back again to this Marshfield Bargain House, and those companies I mentioned between the Marshfield Bargain House and the Medford Bargain House. Does the Alaska Junk Company own any proprietary interest in any of them?

A. No, sir.

Q. Mr. Schnitzer, were you ever a bookkeeper at the Alaska Junk Company?      A. Yes, I was.

Q. Between what years?

A. From the end of 1928 to 1934.

\* \* \*

By Mr. Jones:

Q. Mr. Schnitzer, did you ever receive from the Oregon Steel copies of its balance sheets after the sale was made?      A. Yes.

Mr. Jones: I should like to have these marked in this order (handing document to Clerk).

The Clerk: The first one is Exhibit 30.



(Testimony of Manuel Schnitzer.)

(The document above-referred to was marked  
Petitioner's Exhibit No. 30 for identification.)

Q. (By Mr. Jones): I am handing you Petitioner's 30, and ask you how that came into your possession the first time, and where you saw it?

A. We requested the Oregon Steel Rolling Mills to send us their statement.

Q. Did you have any right to a statement of the Oregon Steel Rolling Mills?

A. We had a right to see them every year.

Q. On what basis?

A. On the basis of the stockholders.

Q. Did it have anything to do with the mortgage?

A. Yes. The R.F.C. had an agreement, on which we were liable to pay a certain percentage of the profit to the R.F.C., and we agreed to pay for the balance, if any; and therefore we protected ourselves by demanding a statement every year of their balance sheets to see that they properly made their settlements.

Q. By "they" you mean the Oregon Steel Mill?

A. Yes.

Q. That is the second and third mortgage?

A. Yes; and also to pay for the first mortgage in a quicker time.

Q. How did that come to you, Exhibit 30?

A. This came to us through their attorney, that is, [200] the attorney for Oregon Steel.

Q. And who was that. A. Mr. Sabin.

The Court: It came to whom?

(Testimony of Manuel Schnitzer.)

The Witness: It came from the attorney of Oregon Steel.

The Court: To whom?

The Witness: To the Alaska Junk Company.

Mr. Jones: We offer Exhibit 30 in evidence.

The Court: That is identified by the witness as what? A balance sheet?

Mr. Jones: As a balance sheet of the Oregon Steel as of November 30, 1944.

The Court: Is there any objection?

Mr. Marcussen: No objection.

The Court: It will be admitted as Petitioner's 30.

(The document heretofore marked Petitioner's 30 for identification received in evidence.)

Q. (By Mr. Jones): I will hand you now another document which I will ask the Court to mark as Petitioner's 31, and ask you to state what that is?

A. That is the balance sheet and profit and loss statement for the year 1945 for the Oregon Steel Mill.

Q. How did that come into your possession?

A. That was handed to us or given to us through our attorney—through Mr. Sabin to the Alaska Junk Company.

Q. Under the same circumstances that you testified with respect to Exhibit 30? A. Yes.

Mr. Marcussen: Counsel may I ask what is the purpose of these offerings?

(Testimony of Manuel Schnitzer.)

The Court: That is for the year 1945?

Mr. Jones: Yes, your Honor.

Mr. Marcussen: What is the purpose?

Mr. Jones: The purpose of this is to show that even in new hands, for a period of time the mill was not successful, and then it finally realized all the optimism that Mr. Morris Schnitzer had in it, that there was real merit behind his idea, but because of increasing prices and difficulties they had to sell it, and even the new owners took two years before they got going.

Mr. Marcussen: I have no objection.

The Court: It will be received.

(The document above-referred to was received in evidence and marked as Petitioner's Exhibit 31.)

(A document was marked as Petitioner's Exhibit No. 32 for identification.)

Q. (By Mr. Jones): I hand you Petitioner's 32, and ask you to state [202] what that is?

A. This is a statement of the Oregon Steel Mills as of December 31, 1946, sent to the Alaska Junk Company through their attorney, Mr. Sabin.

Q. And are the circumstances surrounding your receipt of this the same as with respect to Exhibit 30?      A. Yes.

Mr. Jones: We offer exhibit 32 in evidence, and for the same purpose.

Mr. Marcussen: Just a moment, please. With

(Testimony of Manuel Schnitzer.)

respect to all these exhibits, the Respondent thinks they are immaterial, but we have no objection to the introduction of the others prior to this one which is offered as 32. This is not a balance sheet; it contains a detailed analysis of cost, and so forth, but no balance sheet, and therefore it certainly can have no bearing on the case.

The Court: For what year?

Mr. Marcussen: 1946.

The Court: Three years after the date, and the matters contained therein do not constitute balance sheet?

Mr. Marcussen: That is right. My objection is not based upon the date.

The Court: I think it is rather remote. I will sustain the objection to the one last offered.

(A document was marked as Petitioner's Exhibit No. 33 for identification.) [203]

Q. (By Mr. Jones): I hand you now Petitioner's 33 and ask you to state what that is.

A. This is a balance sheet and profit and loss statement dated in 1946 of the Oregon Steel Rolling Mills, sent to us by their attorney, Mr. Sabin.

Q. Did you get that under exactly the same circumstances as testified with respect to Exhibit 30?

A. Yes.

Mr. Jones: We offer it in evidence for the purposes already stated.

The Court: What year?

Mr. Jones: It is 1946; but it is the balance

(Testimony of Manuel Schnitzer.)

sheet, as to which he objected on the other one, because it was not contained therein.

Mr. Marcussen: I wish to make a statement. I offer no objection so far as the date is concerned, but I think it is wholly immaterial for what it is offered. It is simply a showing that these people may have had a misfortune in dealing with the steel company.

The Court: Exhibit 32 will be excluded, and the record will show what is in it. Petitioner's 33 is admitted.

(The document heretofore marked Petitioner's Exhibit 33 for identification, received in evidence.)

Mr. Jones: I wonder if we can take a five minute [204] recess.

The Court: Yes. We will take a five-minute recess.

(Recess.)

Q. (By Mr. Jones): Mr. Schnitzer, while you were manager at the steel mill, did they keep Mr. McGonigle on the job?

A. They kept him until the mill started to work.

Q. Mr. McGonigle is the representative of the R.F.C.?

A. That's right.

Q. Did you ever prepare any vouchers for payment out of R.F.C. funds for amounts owing Alaska that Mr. McGonigle or the R.F.C. would not pay?

A. We did that continuously.

Q. Did you try more than once to get your account with Alaska paid?

A. Yes.



(Testimony of Manuel Schnitzer.)

Q. Why didn't you get them paid?

A. Mr. McGonigle would not Okeh the payments, and we could not.

Q. Did he have any power over the checking account? A. He countersigned the checks.

Q. Now, from your experience down there, and after you took over, was the mill being built for what the estimate was—the estimated cost? [205]

A. It cost over the estimate.

Q. Could you pay out any of the R.F.C. funds without its consent? A. No, sir.

Q. How did you expect to have that Alaska Junk Company bill paid?

A. We expected to be operating sooner than we did, and pay it off from the profits.

Q. How much were your estimated profits?

A. Our estimates were \$50,000.00 a month.

Q. Would that have been sufficient to have made any payments on the Alaska Junk Company bill?

A. Yes.

Mr. Marcussen: I'll object to that as calling for a conclusion of the witness.

The Court: Go ahead and answer.

A. That would have paid it off nicely.

Q. (By Mr. Jones): Did you, before going down there, have any experience in steel mills?

A. No.

Q. Did any member of your family, or the Wolf family, have any prior experience in steel mills?

A. Morris was the only one that had built up

(Testimony of Manuel Schnitzer.)

a little knowledge about it. He didn't have any actual experience. [206]

Q. He had done some research on it?

A. He had had some research and engineering advice.

Q. Were there any stockholders of the Oregon Steel that had any experience? A. No, sir.

Q. Or officers? A. No, sir.

Q. Or partners of the Alaska Junk; had they any experience with steel mills or smelter work?

A. No.

Mr. Marcussen: The same objection to all this line of inquiry.

The Court: I will overrule the objection.

Q. (By Mr. Jones): Now, after you got there, were there any attempts made to hire experienced people? A. Yes.

Q. What was the result?

A. We were unable to get them.

The Court: Didn't you testify about that yesterday?

Mr. Jones: I think it was his brother.

The Court: All right. Go ahead.

Q. (By Mr. Jones): Were there any attempts to get experienced people?

A. We tried to get several. [207]

Q. After you went in there? A. Yes.

Q. How long did those efforts continue?

A. They continued up until September, 1943; in fact, October of 1943.

(Testimony of Manuel Schnitzer.)

Q. Now then, I am not sure that I asked you this question: What was the situation with respect to creditors before the sale was made to Hall and Mears?

A. Creditors were demanding payment.

Q. Were you able to pay them?

A. No, sir.

Q. What conclusion did the partners of Alaska Junk arrive at with respect to their ability to carry on?

A. We felt we could not handle the situation.

Q. Did you have any agreement to that effect among yourselves?      A. Yes.

Q. You testified yesterday with reference to some people who were contacted with reference to the sale?      A. Yes.

Q. You mentioned Edgar Kaiser and some other people?      A. Yes.

Q. Now, what was the reason for Alaska Junk Company partners going into this, in the first place?

A. We went into it in order to have a good market for [208] scrap, and also to obtain new steel from the mill, which was very difficult to get.

Q. Now, with respect to the purchases that you made on behalf of the Oregon Rolling Mills, or the payments that you made for purchases that the mill had made, that is, the Oregon Mill——

The Court: You are using two different terms. Do you mean the Oregon Steel?

Mr. Jones: Yes, the Oregon Steel.

(Testimony of Manuel Schnitzer.)

The Court: All right.

Mr. Jones: I will reframe the question.

Q. (By Mr. Jones): In respect to payments made by Alaska for orders placed directly by Oregon Steel and Alaska paying the bills, what was the Reconstruction Finance Corporation's attitude toward allowing you to be reimbursed?

A. Would you repeat that question?

Q. Yes. You made advances in order to pay for merchandise ordered by Oregon Steel?

A. Yes.

Q. And you charged those on your account with Alaska? A. Yes.

Q. In order to get payment for this during the construction period would R.F.C. permit the payment?

A. For a long time they would not. And finally we [209] did get, I think it was, several payments; I think it was \$114,000.00.

Q. Which they permitted you to reimburse yourselves for? A. Yes.

Q. In getting them to permit those reimbursements, what did you point out to the R.F.C.?

A. We told them that if they didn't allow us to get our money back we would not give the mill the benefits of our purchasing power, and they would have to obtain it themselves and pay higher prices. In other words, it would be economical for the mill for us to buy it for them, but if we didn't get paid for it, we would refuse to buy it for them.

(Testimony of Manuel Schnitzer.)

Q. Is that the reason they permitted you to be reimbursed?      A. That is right.

Q. Now, the third mortgage that we spoke of yesterday—I may have asked this question but I cannot remember whether I did—the third mortgage that you got from the R.F.C. after the sale, after Mr. Mears and Mr. Hall got the stock—what was the third mortgage applied on?

A. We did not get the third mortgage from the R.F.C.

Q. You are right there. After the sale to Hall and Mears of the stock, the third mortgage from Oregon Steel is [210] what I am talking about; what did that apply on?

A. It was the compromise settlement on the open account.

Mr. Marcussen: If your Honor please, I move to strike the answer on the ground that it is all covered in the stipulation specifically; all of the transaction that he is just testifying about.

The Court: If it has been covered already, don't repeat it.

Mr. Jones: I don't recall whether it is in the stipulation.

Mr. Marcussen: It is stipulated exactly what these notes were given for.

The Court: Well, it won't be stricken this time.

Mr. Jones: May the answer stand?

The Court: It will stand this time, but please don't repeat.



(Testimony of Manuel Schnitzer.)

Mr. Marcussen: May I ask counsel, do you take anything by the answer in addition to the stipulation?

Mr. Jones: No.

Mr. Marcussen: To the extent that there is any inconsistency between his last testimony and the stipulation, of course, his testimony may be disregarded.

Mr. Jones: Sure; if there is any. I don't think there is any.

Mr. Marcussen: I don't know either, but [211] I want to make that clear.

\* \* \*

### Cross-Examination

By Mr. Marcussen:

Q. Now, Mr. Schnitzer, you stated on your direct examination this morning, that Mr. McGonigle of the R.F.C. had charge of the R.F.C. disbursements on this loan, and declined to permit any application of the loan to advances by the Alaska Junk and Morris Schnitzer? A. That is right.

Mr. Marcussen: If your Honor please, I would like to offer in evidence certain documents concerning which [220] I wish to interrogate the witness.

The Court: Does counsel for the petitioner know what they are? You might discuss it with him off the record.

Mr. Marcussen: Yes, I would like to.

The Court: Off the record.

(Discussion off the record.)

(Testimony of Manuel Schnitzer.)

Mr. Marcussen: If your Honor please, I would like to offer as Respondent's exhibit next in order, the balance sheet of Oregon Steel.

The Court: As of what date?

Mr. Marcussen: As of August 31, 1943.

The Court: Is there any objection?

Mr. Jones: No objection.

The Court: It will be admitted as Respondent's X.

(The document above-referred to was received in evidence and marked Respondent's Exhibit X.)

Mr. Marcussen: And as Respondent's Exhibit next in order, the balance sheet of Oregon Steel dated June 30, 1943.

The Court: Is there any objection?

Mr. Jones: No objection.

The Court: It will be admitted as Respondent's Y.

(The document above-referred to was received in evidence and marked Respondent's Exhibit Y.) [221]

Mr. Jones: I do have objection to some things in the folder that I know nothing about; there are some things left in the folder that I know nothing about.

Mr. Marcussen: And as Respondent's Exhibit next in order the balance sheet of Oregon Steel dated May 31, 1943.

(Testimony of Manuel Schnitzer.)

The Court: Is there any objections?

Mr. Jones: No objection.

The Court: It will be admitted as Respondent's Z.

(The document above-referred to was received in evidence and marked Respondent's Exhibit Z.)

Mr. Marcussen: Now, if your Honor please, I would like to ask leave to have them handed to the Clerk and stamped, and then substitute copies.

The Court: Copies will be made for counsel?

Mr. Marcussen: Yes, indeed; copies will be made for counsel.

I think that is all at the present time, your Honor.

The Court: You may proceed with the cross-examination.

Q. (By Mr. Marcussen): I just asked you about the R.F.C. declining to permit the application of the loan to advances made by Alaska Junk and Morris Schnitzer. [222] A. Yes.

Q. Do you recall when the first advances were made on the loan?

A. You mean the first payments of the R.F.C.?

Q. Yes?

A. Not particularly. I didn't come in there until 1943, January, to the mill.

The Court: Doesn't the stipulation disclose that?

Mr. Marcussen: I am just checking it, your Honor.

Q. (By Mr. Marcussen): I show you Exhibit

(Testimony of Manuel Schnitzer.)

No. 12, offered in evidence in this proceeding, which is the Mortgage Payable account of Oregon Steel, the "Mortgage Payable," referring, of course, to the R.F.C. mortgage and loan, and I call your attention to the first entry, which is under date of November 30, 1942, showing a credit to the mortgage in the amount of some \$27,000.00. I believe you testified, and I think counsel will agree with me in this, that that item represented the first advances from the R.F.C. which were made some time prior to that, probably in the month of November. Bearing that in mind, can you identify the time of your conversation with Mr. McGonigle about his functioning to approve loans and his refusal to approve the payments of any of the so-called open accounts of Morris Schnitzer and Alaska Junk?

A. I didn't have any talk with Mr. McGonigle before [223] January, 1943.

Q. You didn't have any talks with him before January, 1943? A. That is right.

Q. At the time you came into the picture, in January, 1943, Mr. McGonigle was already then functioning in that capacity; is that correct?

A. Yes.

Q. And do you know how long prior to that he had been passing on the disbursements which were to be made for funds provided in the loan?

A. He was on the job when they started disbursements from the R.F.C.

(Testimony of Manuel Schnitzer.)

Q. Right from the beginning? A. Yes.

Q. And do you know whether Morris Schnitzer, or any of the principals of the Alaska Junk Company had ever been given any reason to believe by the R.F.C. that the R.F.C. loan would be for the purpose of paying off any advances that either Morris Schnitzer or Alaska Junk would make to the corporation? A. Would you repeat that?

Mr. Marcussen: Will you read the question, please, Mr. Reporter?

(Whereupon, the last question was read by the reporter [224] as above recorded.)

A. What promises the R.F.C.—as I understand the question, it is whether the R.F.C. had made any promises to the principals whether they would pay any of the advances made?

Q. Promises or representations of any kind?

A. I don't believe I would know about that.

Mr. Jones: What was the answer?

The Witness: I don't believe I would know about that.

Q. (By Mr. Marcussen): You didn't know about that? A. No.

Q. Didn't you testify in your direct examination that the reason why this open account, so-called, of both the Alaska Junk and Morris Schnitzer was not paid, was that the R.F.C. declined to permit disbursements of its loan for the purpose of making this payment? Didn't you testify to that? A. Yes.



(Testimony of Manuel Schnitzer.)

Q. You apparently know something about that.

A. I know they refused to pay the bills of the Alaska Junk Company.

Q. But you know nothing of any representations that the R.F.C. may have made, which may have given the Alaska Junk or Morris Schnitzer any reason to believe that any of [225] those open accounts would be paid with R.F.C. loans?

A. As a matter of fact, they did pay \$114,000.00 worth.

Q. What \$114,000.00 worth was that?

A. I believe those items were on the original estimate to the R.F.C. the equipment that would be in the original estimate of the cost that we gave them to build the mill.

The Court: When was the \$114,000.00 paid? Over what period?

The Witness: They were made in two or three payments.

The Court: Was that before or after you came there?

The Witness: A part of it was after I came there, and a part of it was before.

Q. (By Mr. Marcussen): How much was before, and how much was after?

A. Well, let's see——

Q. By the way, what was the date to which "before" and "after" apply?

A. We are talking about before and after January, 1943.

(Testimony of Manuel Schnitzer.)

Q. I will withdraw my question and rephrase it. You testified on your direct examination that first the R.F.C. declined to permit application of its loan to Alaska Junk and Morris Schnitzer accounts?

A. After January, 1943; I was not down at the mill and didn't have much to do with it before that time.

Q. Now, when was it that they permitted the application [226] of this \$114,000.00?

A. You just showed me the sheet, which was in November, 1942.

Q. Now; this sheet does not show that (indicating). A. It does not?

Q. I am asking you about your testimony concerning the \$114,000.00 that the R.F.C. finally agreed might be paid from the funds advanced by it on its R.F.C. loan—might be paid on the account of Alaska Junk and Morris Schnitzer? A. Yes.

Q. Now, when was it that the R.F.C. consented to make that advance or that payment of \$114,000.00.

A. I don't know.

Q. Did any of the \$114,000.00 pertain to any payment which had already been made on the Alaska Junk—I beg your pardon. I will withdraw that question. I think the evidence will show, and I think it is safe to assume that at the time the R.F.C. consented to the application of the \$114,000.00 of its loan to the payment of advances by Alaska Junk and Morris Schnitzer, that substantial advances had already been made at the time by both

(Testimony of Manuel Schnitzer.)

Morris Schnitzer and Alaska Junk; do you have any doubt about that?      A. No.

Q. And at the time the \$114,000.00 was authorized to be applied on the account, how much of that which was applied [227] to the account first was already on the books and how much of it was applied to any future advances?      A. I don't know that.

Q. You don't know that?      A. No.

Q. Do you have any idea what those proportions might be?      A. No, sir.

Q. Do you know whether any part of the loan was to apply at all to past advances?

A. I assume they were; I don't know.

Q. But you don't know.      A. No.

Q. Didn't you state that in discussing this matter with the R.F.C. that you pointed out to them in substance, that if they would not authorize you to use R.F.C. funds to pay advances, which might be made by Morris Schnitzer and Alaska Junk to the corporation, that the corporation would be at a disadvantage, and that you would withdraw the advantage, that is, Alaska Junk and Morris Schnitzer would withdraw the advantage by reason of their purchasing power, and thereby any purchasing power advantage which Oregon Steel may have gotten as a result of those advances being made by Morris Schnitzer and Alaska Junk would be lost? Do you recall that?      9. Yes. [228]

Q. Would you refresh your recollection as to their agreement to apply R.F.C. funds to future advances or to past advances?      A. How?

(Testimony of Manuel Schnitzer.)

Q. Well, was the question ever brought up? Was the agreement with respect to future advances, or past advances?

A. That doesn't help to refresh my recollection any.

Q. Were you here in the courtroom yesterday when your brother Morris Schnitzer testified?

A. Yes.

Q. Do you recall some testimony on his part in a similar vein with respect to the refusal of the R.F.C. to permit application of its loan to these accounts?

A. Yes.

Q. Your answer is that you do? A. Yes.

Q. Now, from what you know of the finances of this company can you offer any explanation as to how the items would otherwise be paid for,—strike that. Now, the R.F.C. loan was applied to certain payments, most of which did not go to Alaska Junk and Morris Schnitzer; is that so?

A. That is true.

Q. If the R.F.C. loan had been used to pay the open account of Alaska Junk and Morris Schnitzer, where would the funds have come for the payments by the R.F.C. loan which [229] the R.F.C. loan was supposed to be used for?

Mr. Jones: I will object to that as hypothetical.

The Court: The hypothetical part links Morris Schnitzer with the Alaska Junk. I didn't know he was interested with the Alaska Junk; I thought he was manager of the Oregon Steel and not the Alaska Junk.



(Testimony of Manuel Schnitzer.)

Mr. Marcussen: That is correct, your Honor.

The Court: I think the question was about the advances by Morris Schnitzer and Alaska Junk?

Mr. Marcussen: That is correct; that is what is in issue.

The Court: I didn't think Morris Schnitzer had anything to do with that?

Mr. Marcussen: Oh, yes; it is in the stipulation.

The Court: I thought he was on the receiving end and not the giving end.

Mr. Marcussen: And this witness has also testified concerning the application of the R.F.C. loan.

The Court: All right. Suppose we have the question.

Mr. Marcussen: Will you read the question to the witness, please?

(Whereupon, the last question was read aloud by the reporter as above recorded.)

The Court: I will overrule the objection. [230]

Q. (By Mr. Marcussen): Do you understand the question?

Mr. Jones: May I save an exception to that ruling?

The Court: Yes.

Mr. Jones: May I state my position on it more fully?

The Court: Go ahead.

Mr. Jones: It is a hypothetical question, based upon an hypothesis with respect to something existing that did not exist, and then he follows that with



(Testimony of Manuel Schnitzer.)

asking where would certain funds have come from to do something with. I think it is completely out of range of anything that he testified to on direct examination; it calls for a conclusion,—not even a conclusion, but a speculation of something almost unintelligible.

The Court: I think in cross-examination counsel should be permitted to search. Of course, in redirect examination, if there is anything that needs to be cleared up, you may do so.

Mr. Marcussen: So that you may better understand the nature of the inquiry that I am making at this time, I wish to point out that both the testimony of this witness and the witness Morris Schnitzer contains the implication that somehow or other Alaska Junk and Morris Schnitzer were led to believe that their advances on open account to the corporation, [231] Oregon Steel, would be paid from the funds which were advanced by R.F.C.; and it will be shown here that there was and there could not have been any such expectation. I am now asking the witness about that matter to which he himself has testified.

The Court: Ask him first if he understood that funds were to be applied to that.

Mr. Marcussen: I have asked him that, I believe.

The Court: Ask him that, and then go on to the next question.

(Testimony of Manuel Schnitzer.)

Q. (By Mr. Marcussen): Do you understand the question, Mr. Schnitzer? A. Which one?

Q. The last question.

The Court: Ask him if he understood that the premise was correct, or whether your premise was correct; ask him that question.

Mr. Marcussen: Very well.

Q. (By Mr. Marcussen): Is it your understanding that the purpose of the R.F.C., either in whole or in part, was to advance funds to pay off the advances which had been made by Morris Schnitzer and the Alaska Junk Company?

A. I think the purpose of the R.F.C. loan was to complete the mill. [232]

Q. Yes. And will you answer the question, please?

A. Will you give it to me again, please?

Mr. Marcussen: Will you read it, Mr. Reporter?

(Whereupon the question referred to was read by the reporter as follows: "Is it your understanding that the purpose of the R.F.C., either in whole or in part, was to advance funds to pay off the advances which had been made by Morris Schnitzer and the Alaska Junk Company?")

The Court: What is the answer to that question?

A. I believe that was the general purpose of the loan.

Q. (By Mr. Marcussen): Now then, I want to go on to the next question which has been in con-

(Testimony of Manuel Schnitzer.)

troversy, and on which the Court has ruled you may answer; and I will ask you if the R.F.C. funds had been used to pay off the advances by Alaska Junk and Morris Schnitzer to Oregon Steel, where would the funds have come from or where might they have come from, or where was it anticipated by the parties that these funds would come from to pay for the items that the R.F.C. funds were actually used to pay for?

A. First, our purpose was that the mill would start running before it did; and, naturally, we thought it would run successfully, and that would take care of a part of it; secondly, we discussed trying to get another loan from the R.F.C.,—an additional mortgage. [233]

Q. You did get an additional mortgage?

A. Of \$100,000.00, yes, we did; and we were trying to get another one.

Q. But it was realized, was it not, that there would have to be some funds applied in the manner in which the R.F.C. funds were actually applied, was it not?

A. Yes, it was.

Q. Now, you testified as to the third mortgage, and counsel and I had some conversation which you may remember about material contained in the stipulation in the same item. I think you stated that the third mortgage, which was finally received by both Morris Schnitzer and the Alaska Junk, was used, in part, to pay the open account.

(Testimony of Manuel Schnitzer.)

A. Compromise settlement of the open account.

Q. Do you know that the money advanced by the corporation, or, rather, the loan advanced by the corporation in the third mortgage was actually used to pay notes representing that open account?

A. I don't know what you mean by that.

Q. You don't understand the question?

A. No. [234]

\* \* \*

Q. (By Mr. Marcussen): You made some statement in your direct testimony, as I recall, Mr. Schnitzer, pertaining to the fact that one of the reasons for establishing Oregon Steel was to obtain new steel and to provide a market for scrap with the Alaska Junk. Do you recall that? A. Yes.

Q. And was there a large demand for scrap at that time? [245]

A. In 1940 and 1941? There is always a market for scrap.

Q. Was it a good market?

A. Not very good.

Q. What would be the price of scrap at that time?

A. In 1940 and 1941; is that what you mean?

Q. Yes?

A. I believe it was ten or twelve dollars a ton.

Q. How did that compare with prices, we will say, the last five years previous?

A. Oh, we have had higher markets and we have had lower markets.



(Testimony of Manuel Schnitzer.)

Q. During the five years previous?

A. Yes; markets can change in a week. We have had changes in the last few months, changes of from eight to ten dollars a ton.

Q. During the year 1941, towards the end of the end of the year, was there ever any serious concern on the part of the Alaska Junk Company and Morris Schnitzer concerning outlets for the sale of scrap metal at that time in history?

A. No; we were not concerned about it; but what we were concerned about was to have a market that we would have an advantage over our competitors. It is a very competitive business, the scrap business is. In other words, if you have a customer where you can get a one dollar a ton advantage [246] over the other man, you can do more business that way.

Q. I see. It was proposed that Oregon Steel be that customer?

A. I don't know what you are talking about. With Oregon Steel, we would be in a favorable position with them.

Q. Now, do you know why it was in 1943 that Oregon Steel was unable to pay its creditors, as you testified?

A. Due to the conditions that I previously outlined; we did not have the money to pay the bills.

Q. Had it been a long-standing ambition of your father to establish Morris Schnitzer in the steel business?



(Testimony of Manuel Schnitzer.)

A. What kind of a steel business do you mean?

Q. The very business that he eventually went into?

A. Into the Oregon Steel mill?

Q. In a steel business?

A. I don't think he was displeased that he was in that business.

Q. That is not what I asked you.

A. Was it his ambition?

Q. Do you know whether it had been a long-standing ambition of your father, a dream as it were of your father, to establish your brother Morris in the steel business?

A. I think it was his ambition, yes.

Q. Now, you remember many conversations that have taken place. What did your father say about it? [247]

The Court: I don't see the necessity of going into the details of the conversation; I think the fact that he had that ambition is sufficient; it won't make any difference what the conversations were.

Mr. Marcussen: All right.

The Witness: My father had ambitions for all the family.

Mr. Jones: There has been a ruling.

Mr. Marcussen: I will withdraw the question.

Q. (By Mr. Marcussen): Now, with respect to the Marshfield Bargain House; how did you identify that organization?

A. Marshfield Bargain House?

Q. Yes? A. They are in Eugene.

(Testimony of Manuel Schnitzer.)

Q. Eugene, Oregon?

A. Pardon me; Marshfield, Oregon. They were in the scrap business, and also sold machinery, and so forth.

Q. Who owned that business?

A. That belonged to Morris Rubenstein and his partner; it was Rubenstein and Schneiderman.

Q. Were they engaged in a partnership?

A. I am quite sure they were; I think they were. I am quite sure it was a partnership. It might have been a corporation, but I think it was a partnership.

Q. What did you understand proprietary interest to be?      A. In a partnership?

Q. Well, can you answer the question as I asked it?

A. I don't know what you mean. Is there any other way that you can ask the question?

Q. No.

A. What do I understand it is; my understanding a proprietary interest in a partnership is that a man is a partner in the business.

The Court: I think that is a question of law. I don't think that is important here.

Q. (By Mr. Marcussen): Now, at the beginning of your testimony today you made a reference to numerous organizations to which finances had been given or advanced by Alaska Junk. I would like to have you take the first of those that you mentioned today, which was M. Turn; I think that is the first one you mentioned.

(Testimony of Manuel Schnitzer.)

A. I don't remember which one was the first one.

Q. Let us take M. Turn. I think you stated that you made an advance to M. Turn? A. Yes.

Q. What kind of a business did he operate?

A. The same kind as the Marshfield Bargain House.

Q. Who operated the business?

A. Mr. Max Turn. [249]

Q. What was the purpose of advancing him money?

A. He would come and say, "I will give you some scrap iron if you will advance me \$500.00 to finance a deal that I have where I can get some."

Q. The purchase of scrap that was eventually to be delivered to Alaska Junk?

A. That is right.

Q. Were there ever any other advances made to that company, or to that individual?

A. We made several advances to him.

Q. For the purpose which you have just described? A. Yes.

Q. Any other purpose?

A. That is the only purpose.

Q. Now, how about Munce and Pedrante?

A. Munce and Pedrante,—they didn't have too much money, and we would give them the money and they would buy a deal and haul it in to us; we would give them the money in advance, and then they would work it out partially, or, there would be an advance made to partially cover it, for the purpose of helping them out currently.

(Testimony of Manuel Schnitzer.)

Q. Currently on what?

A. On the loads that they brought in.

Q. To Alaska Junk? A. That is right.

Q. Did you testify concerning any advances that Morris Schnitzer made to any of these companies?

A. No, I did not.

Q. Now, then can you name any other company that you mentioned this morning?

A. Industrial Air Products.

Q. What was the nature of the advances made to them?

A. Well, Sam Schnitzer, and Rose Schnitzer, and Jennie Wolf and H. J. Wolf, and Morris Schnitzer started that corporation at the end of 1938, in the beginning.

Q. What about it?

A. Well, I think it went into operation around the beginning of 1939, for the purpose of manufacturing oxygen and acetylene, and for the sale of welding supplies.

Q. Did you say that was a corporation?

A. Yes.

Q. It was a corporation? A. Yes.

Q. And is that stock shown as an asset on the books of Alaska Junk? A. No, it is not.

Q. Were the advances that you referred to advances made for the payment of stock in the company?

A. They were for payment of stock; and also

(Testimony of Manuel Schnitzer.)

the cost went more than the expected cost, so the Alaska Junk made some [251] more advances. We sold them more merchandise for the building and plant, like pipe, and steel, and so forth.

Q. What did Alaska Junk receive for their advances?

A. They eventually received stock, and eventually got paid back for the sales and advances made to them.

Q. Now, can you name another company that you referred to this morning?

A. I think we mentioned the Hesse Ursted Company.

Q. What was the nature of the advances made to them?

A. We made cash payments for them; and we got a mortgage from them, I think it was, for \$50,000.00, or \$60,000.00. They were in the hands of receivers, or in the court, and they were practically closed up, and we advanced them this money, and they gave us a mortgage for the plant; and through this operation they purchased a tremendous amount of material for us, and we received the benefits of a part of the profits of the deal that they made. They had a Government property, and we got one-third of the property,—the profits on it.

Q. You mean the profits that were applied to the loan?

A. No; we got that as extra profits. The loan, they paid that with interest.



(Testimony of Manuel Schnitzer.)

Q. When did they go into bankruptcy or receivership? A. I think it was in 1941.

Q. At the time they were financially embarrassed in that [252] manner, did they owe you any money, Mr. Schnitzer? I mean, did they owe Alaska Junk any money? A. No.

Q. Did Alaska Junk sell them anything up to that time? A. Very little.

Q. Who made the proposal to Alaska Junk that they go into the picture, as you have described it?

The Court: I don't think the detail is material. You need not answer that.

Mr. Marcussen: If your Honor please, I want to get a complete description. He testified to it on direct examination.

The Court: There is no use getting all the details of the transactions, but just the main parts.

Q. (By Mr. Marcussen): The loan was made after they were financially embarrassed?

A. Yes.

Q. What was the full agreement pertaining to the making of that loan?

A. What do you mean?

Q. Specifically, did it have anything to do with the profit that you might get out of it?

A. We were going to get paid the mortgage and interest. [253]

Q. I think you said something about a profit that you were to get on certain deals?

A. And later a chance came up for a government

(Testimony of Manuel Schnitzer.)

job, on which we had put up a bond, and we signed for the application, in order to complete the job, that is, a performance bond; and we got one-third of the profits.

Q. What kind of a contract with the government? A. It was to complete the job.

Q. In other words, the Alaska Junk joined with Hesse and Ursted in bidding on a contract for the government?

A. That is right; we were on the bond.

Q. Did you advance funds, or did you just go on the bond? A. We went on the bond.

Q. After going on the bond, the agreement was that you were to get one-third of the profits?

A. That is right.

Q. Did Alaska Junk, with respect to the same contract, have anything to do with the actual operation of the contract or the performance of it, other than you described?

A. We guaranteed that they would complete the job; we sold them a lot of material for it.

Q. Now then, there was another organization that you mentioned, a Mr. Nyberg?

A. Nyberg. [254]

Q. Did you testify that advances were made by Alaska Junk to Nyberg? A. Yes.

Q. What was the nature of those advances?

A. It was in the dismantling of a railroad.

Q. What railroad?

A. I believe it was over at Stevenson.

(Testimony of Manuel Schnitzer.)

Q. Oregon? A. In Washington.

Q. And did Alaska Junk have a contract to purchase the scrap of that job?

A. No. He was dismantling; we had a contract with him to do the labor on that job.

Q. Did you get any of the scrap on that job?

A. Oh, yes.

Q. What was the purpose of the advance?

A. We gave him the advance so that he could meet the payrolls and pay expenses.

Q. That is, for that particular job?

A. That's right.

Q. So that you could get the scrap?

A. Yes.

Q. Now, what other company did you testify about this morning?

A. I think I mentioned the Steel Tank and Pipe Company [255] of Portland.

Q. And when were advances made to it?

A. I believe that was in 1932 or 1933.

Q. And what was the nature of those advances?

A. We purchased the boiler works; the Birchfield Boiler Works in Tacoma.

Q. As a salvage proposition?

A. No; they didn't have the money to buy it, and they came over to us and asked us if we would buy it for them, and we went up to Tacoma two or three times, and the Birchfield Boiler was in the hands of the Court, and finally were the successful bidders on that, and we made an agreement with

(Testimony of Manuel Schnitzer.)

the Steel Tank and Pipe to turn it over to them, and sell them materials. Also, they were to sell us materials. They paid us off in materials, principally.

Q. They were to pay you off in scrap, was that it?      A. That's right.

Q. Had you ever purchased scrap from them before?

A. Yes; we had been buying from them before.

Q. Can you name another company that you mentioned this morning?

A. We had the National Machinery Company.

Q. The National Machinery Company?

A. Of Eugene.

Q. What was the nature of the advances made to that [256] company?

A. That was a company that we advanced money and materials and supplies to.

Q. Who owns that company?

A. That company belonged to Sam Schnitzer, H. J. Wolf, Rose Schnitzer, Jennie Wolf, and Mr. Roy Nehl; he had an interest in it.

Q. What was the relative interest of Mr. Nehl?

A. I believe he got ten per cent of the profits.

Q. For his services?

A. For his managing services; yes.

Q. In other words, he had a bonus; is that it?

A. Yes, a bonus arrangement.

Q. Was it a corporation?

A. I think it was.

(Testimony of Manuel Schnitzer.)

Q. And when you referred to advances to that corporation, are you referring to the money paid for the stock?

A. No, not the stock; we had sold them a lot of merchandise.

Q. You did sell them merchandise?

A. Yes.

Q. And what was the nature of the merchandise?

A. Electric motors, wire rope, steel, belting, and so forth.

Q. When you say you made advances for them, you mean [257] that you charged them for those materials?

A. We charged them for the materials that we shipped to them.

Q. That you shipped to them?

A. That's right.

Q. And what was the business of this company?

A. It was in the business of selling sawmill and logging machinery and farm supplies.

Mr. Jones: I realize this is cross-examination, but I am going to have all the records on each of those companies.

The Court: I think that about concludes the collateral matters, anyway.

Q. (By Mr. Marcussen): What other companies did you testify about?

The Court: I want to get to that point and quit for lunch, so as not to go over it again.



(Testimony of Manuel Schnitzer.)

Q. (By Mr. Marcussen): The Central Supply is one you testified about? A. Yes.

Q. What was the nature of those advances to that company?

A. We advanced first of all, a certain amount for capital stock, and after that for merchandise that we sold them. [258]

Q. When you say the advances were made to them, the advances are those advances involved in selling them merchandise on open account?

A. In furnishing them money, also; money and merchandise.

Q. What money? What was that for?

A. We had to organize it; the company had expenses.

Q. You received stock for that? A. Yes.

Q. And who owned the stock?

A. The stock belonged to Sam Schnitzer, Rose Schnitzer, H. J. Wolf and Jennie Wolf.

Q. And what was its business?

A. It was in the business of selling plumbing and electrical materials.

Mr. Jones: If the Court please, I intend to have the accountant on the stand, who can go over this.

The Court: I would like to have him conclude his cross-examination before we quit, so we won't have to go over it again.

Q. (By Mr. Marcussen): In these agreements that you have mentioned, in which you stated a part of the advances were for payment of stock, did

(Testimony of Manuel Schnitzer.)

anybody else own any stock besides the individuals that you have mentioned? That is, that you know of?      A. I don't think so. [259]

Q. I am referring now to substantial holdings, and not qualifying shares?

A. I don't think so.

Q. Do you recall any other company that you mentioned?

A. Plumbing and Heating Sales.

Q. What was the nature of the advances made to that company?

A. We started the company,—I don't mean "we" but Rose Schnitzer, Jennie Wolf, Sam Schnitzer and H. J. Wolf,—they had a man by the name of Mr. Shea, who was in the plumbing and heating installation business. That is a specialized business. In other words, in order to be able to do contract work for installation of plumbing and heating, you had to have a man who knew plumbing and heating. So Mr. Shea was the manager, and he had an interest in that business.

Q. An interest,—you mean by way of a bonus arrangement?

A. I think he had stock in the company.

Q. And the rest of the stock was owned by whom?

A. By the four parties I mentioned.

Q. Was a part of the advances made for the stock in the company?      A. Yes.

Q. The Alaska Junk sold merchandise to the company?      A. Yes. [260]

(Testimony of Manuel Schnitzer.)

Q. Were some of the advances that you testified about as made to that company, advances that arose from the fact that materials were sold to them?

A. We sold them, and bought from them, also.

Q. But insofar as your advances were concerned, they were advances resulting from sales?

A. I don't know whether it was all exactly merchandise; I know there was some merchandise.

Q. You don't know?           A. I don't know.

Q. Did you testify about the Medford Bargain House?           A. Yes.

Q. Have you gone over that? Do you recall?

A. No, we did not.

Q. Can you tell me about the nature of advances to that company?

A. The Medford Bargain House was similar to Max Turn and to the Marshfield Bargain House; exactly the same.

Q. The Alaska Junk or its partners, did they have any stock in that company?           A. No, sir.

Q. Who owned that?

A. That belonged to a Mr. Rubenstein and a Mr. Kaplan.

Q. And were the advances to that company the same as to the other companies that you mentioned? [261]

A. The same as to the Turn outfit and to the Marshfield Bargain House.

Q. For the purposes of enabling them to get scrap iron, so that you could buy the scrap?

(Testimony of Manuel Schnitzer.)

A. To buy the scrap, and so that they could furnish it to us.

The Court: Does that conclude the collateral transactions?

Q. (By Mr. Marcussen): Did you testify about the Vaughan Motor Works?

A. I have not yet.

Q. I mean on cross-examination?

A. I don't think you asked me about it. We just mentioned it; that was all.

Mr. Jones: I did.

Q. (By Mr. Marcussen): What was the nature of the advances made to that company?

A. We advanced them several thousand dollars in the purchase of a mortgage that a party had on that company, and he had put the sheriff out there to close it up, and we bought the mortgage for them, and allowed the Vaughan Motor Works to open up. He had a \$3,000.00 mortgage on this company, and we bought it for \$2,000.00; and we charged the Vaughan Motor Works with the \$2,000.00, although the party [262] wanted us to pay the original \$3,000.00; we would not do it; and they paid us off with merchandise that they manufactured.

Q. Manufactured merchandise that the Alaska Junk needed in its business?

A. That is right.

Q. Were there any other advances made to that company?

A. That is the only one.

(Testimony of Manuel Schnitzer.)

Q. What about the advances to Carlton Coast Liquidators?

A. We advanced them large sums of money, and also equipment and supplies and things that they needed.

Q. And the equipment and supplies were sold to them; is that right?

A. Yes, that is right.

Q. What was the money advanced to them for?

A. Well, it was a terrific job, I mean, they had to have a lot of help, and it involved labor. We had bad luck in the weather, washouts of bridges, and so forth, and we had to advance money from time to time before the money started coming back.

Q. Was that a corporation? A. No, sir.

Q. At the time the advances were first made, had any business been done by that company with Alaska Junk?

A. Well, the company was not in existence until we formed the company. [263]

Q. I see. Alaska Junk joined with other operators to form that company?

A. With Dulien Steel Products.

Q. How much of an interest did Alaska Junk have in that? A. Fifty per cent.

Q. Who had the other fifty per cent?

A. Dulien Steel Products.

Q. What was the purpose?

A. To dismantle a logging railroad and logging camp; it was railroad equipment, locomotives, and logging cars.



(Testimony of Manuel Schnitzer.)

Q. And did Alaska Junk receive that as scrap?

A. No; that was carried as a separate venture; and whatever was sold went through the Carlton Coast books.

Q. Was that operation substantially the same as the Alaska Junk operation insofar as the purchase and sale of salvage equipment was concerned, and so forth?

A. No; this company just made that one purchase.

Q. And was that one purchase of the same type as was ordinarily entered into by the Alaska Junk Company? That is what I mean.

A. That is right.

Q. Were there any other companies that you testified about?      A. I don't know. [264]

Mr. Jones: Industrial Air.

The Witness: I think we discussed that.

Q. (By Mr. Marcussen): That corporation was formed by the Alaska Junk?

A. Yes; and Morris Schnitzer.

The Court: Are you through with these collateral matters? If you are, we will take a recess for lunch.

Mr. Marcussen: I just wanted to ask him one more general question.

The Court: Are you through with these collateral matters, because I don't want to have to start over them again after lunch.

Q. (By Mr. Marcussen): These advances, gen-

(Testimony of Manuel Schnitzer.)

erally, consisted of advances for stock, where stock purchases were made, and advances that were made in the nature of materials, such as sales?

A. That is right.

Q. And they were made as advances for the purpose of financing a scrap operation or a salvage operation in which the company was interested; and then advances were made on mortgages and that sort of thing from time to time?

A. That is right.

Q. For any other purpose, that you can think of?

A. We gave them either money or materials; that would cover it all. [265]

Mr. Marcussen: I have no further examination along that line; but I would like to continue with the witness this afternoon.

The Court: We will take a recess for lunch.

Mr. Jones: What time shall we come back?

The Court: Will two o'clock be all right?

Mr. Jones: That will be all right.

The Court: All right. We will recess one hour for lunch.

(Whereupon, at 1:00 o'clock p.m., a recess was taken until 2:00 o'clock p.m., same day, same place.) [266]

#### Afternoon Session

The Court: As I understand it, the Respondent had not concluded his cross-examination at the recess?

Mr. Marcussen: No, I had not.

(Testimony of Manuel Schnitzer.)

Whereupon,

MANUEL SCHNITZER

the witness on the stand at the time of the taking of the noon recess, called by and on behalf of the Petitioner, having been previously sworn, resumed the stand and testified as follows:

Cross-Examination

(Continued)

By Mr. Marcussen:

Q. I think, in your direct testimony you made reference to cancellations of certain orders?

A. Yes.

Q. What was the cause of that cancellation?

A. It was cancelled because we delivered a part of it, and the rest of it we were not producing fast enough, and we were running into difficulties.

Q. Did you have any difficulty with your equipment and machinery?     A. Yes.

Q. What items of machinery and equipment were you having difficulty with?

A. Well, the mill motors were not running at the [267] right speed; it required different motors; they were too fast.

Q. Who supplied those motors?

A. Those motors came with the mill that was purchased from the General Cable Corporation.

Q. Who purchased them from the General Cable Corporation?     A. Morris.

Q. Was that purchased by Morris Schnitzer or the Alaska Junk, first?

(Testimony of Manuel Schnitzer.)

A. I don't recall; I think it is in the record; I know that he made the transaction; in whose name, I do not know.

Q. Did he make it during the life of Oregon Steel?

A. I don't know whether he bought it before Oregon Steel was organized, or after; I think the record would show.

Q. What other items of equipment did not function properly?

A. Well, that was an important part. Second, the rolls that we had gave us difficulty; the design of the rolls was not proper; they were not properly designed, and we did not have enough of them on time.

Q. Were they used rolls or new rolls?

A. They were new rolls.

Q. Who were they supplied by? [268]

A. Those were supplied by the United Engineering Works; they supplied most of them, and then there was a few purchased from other companies, but I don't remember their names.

Q. Do you recall your testimony yesterday when you were quoting the accountant of the company to the effect that the company could not afford to lose more than \$125,000.00?

A. Yes; not lose; I didn't say we couldn't afford to lose. We could not afford to invest in the Oregon Steel Rolling Mills.

Q. More than \$125,000.00?

(Testimony of Manuel Schnitzer.)

A. That's right.

Q. What accountant were you referring to?

A. Mr. Schnitzer.

Q. Who? What Mr. Schnitzer?

A. A cousin of mine; an accountant,—an accountant of the Alaska Junk Company.

Q. By the way, is that a brother of Louis Schnitzer? A. Yes; Mr. M. R. Schnitzer.

Q. You testified also about efforts to secure capital from other sources; what other sources? Do you know?

A. At which time are you talking about?

Q. Well, any time during the process of organizing the Oregon Steel.

A. Well, we were,—the one I referred to is to the R.F.C., after the \$700,000.00 loan. [269]

Q. After the loan was granted? A. Yes.

Q. From whom were efforts made to secure capital at that time?

A. We discussed that with Mr. Kennedy.

Q. You mean that efforts were made to secure additional money from the R.F.C.? A. Yes.

Q. And what did Mr. Kennedy say?

A. He didn't think it would go through.

Q. What reason did he give for that?

A. Well, I don't remember the reason; he said in his opinion it would not go through, and since Washington always referred the matter back to the head of the district it was in, it would take his recommendation to put it through.



(Testimony of Manuel Schnitzer.)

Q. Did he say he would not give his recommendation? A. That is right.

Q. Did anybody discuss the reasons with him?

A. I was not the one that did it; so I don't know that I would know the reason for it.

Q. You didn't have any negotiations with him?

A. No, I did not.

Q. I would like to have you refresh your recollection carefully on this: was there any effort made to secure capital from other concerns? [270]

A. Well, before the thing was organized we did discuss this with Dulien Steel Products.

Q. What was the nature of those discussions?

A. Dulien Steel Products was supposed to go into a steel mill.

Q. A steel mill, or Oregon Steel?

A. Into a steel mill; we had not named it yet.

Mr. Jones: I didn't hear that?

The Witness: Into a steel mill.

Q. (By Mr. Marcussen): Was it this steel mill, regardless of whether or not it was named?

A. This was the one that they were contemplating, and then Dulien said he was not interested, that he was working on one of his own. In other words, it was a race, whether we would get in there first, or he.

Q. Were any efforts made to induce the Kaiser interests to get into this corporation, or to get money into this corporation?

(Testimony of Manuel Schnitzer.)

A. During October or November we were negotiating with them to sell the mill.

Q. Had there been any negotiations with them about the possibility of them investing capital in the enterprise?

A. The deal with them was for them to have it entirely.

Q. Now, you said something about the profits that were [271] expected from this enterprise, and you mentioned a figure of \$50,000.00?

A. Yes.

Q. How did you identify that, annually or monthly?      A. \$50,000.00 per month.

Q. What basis did you have for saying that?

A. The engineers, Arthur G. McKee gave us a schedule based on the cost of scrap, the price of electricity, labor, and so forth; and they gave us a quotation of, I believe, around \$30.00 per ton on the ingots, and \$10.00 a ton on the production expense, which would make it \$40.00; and the price at that time was around \$52.00 to \$60.00 per ton on finished steel, which was to leave us a profit of \$10.00 per ton; and we figured it would produce from four to five thousand tons a month.

Q. Did McKee figure you would produce that much, too?      A. Yes.

Q. So that you were to have profits around \$600,000.00 a year?      A. That's right.

Q. How long did the mill actually operate in

(Testimony of Manuel Schnitzer.)

1943, while it was still under the Schnitzer-Wolf ownership?

A. We started making ingots, I believe, in June, —May or June,—and we started rolling at the end of August, and we rolled through September and a part of October. [272]

Q. Now, were those simply test operations?

A. Well, we started to operate; I don't know whether it was test operations.

Q. Did you continuously melt ingots after you once started right on until the end of October?

A. I don't remember the time we started melting ingots.

Q. You could not identify that at all?

A. I think we stopped melting ingots about a week before we finished rolling.

Q. When did you finish rolling?

A. As I said, I think it was around the end of October.

Mr. Marcussen: No further questions.

Mr. Jones: I have one or two questions here.

### Redirect Examination

By Mr. Jones:

Q. Mr. Schnitzer, where was your chief market, or where were your chief markets for scrap in the United States prior to or well along in 1941, 1942 and 1943?

A. Our main customer was Seattle, Bethlehem Steel.

Q. What was the freight rate between Portland and Seattle?      A. Approximately \$3.00 a ton.

(Testimony of Manuel Schnitzer.)

Q. What has the steel mill effect in Portland been on the price of scrap? [273]

A. The price was cheaper in Portland,—not exactly,—the full amount of the freight did not exactly show it. But there was a sort of compromise in the price, being about \$1.50 a ton cheaper than it was in Seattle.

Q. And since the steel mill, what has happened?

A. Same thing; steel, I would say, is exactly the same.

Q. And your selling price?

A. The selling price at Portland or Seattle is the same price.

Q. If you sell, who pays the freight to Seattle?

A. The mill, the Bethlehem Steel, pays the freight there.

Q. Before this mill came in, what was the difference?

A. It was \$1.50 to \$2.00 lower than Seattle.

Q. If I understand you right, the effect of the mill here has been to increase the price of scrap by \$1.50 or \$2.00 a ton?

A. Correct.

Q. Do you know whether that was ever contemplated or thought of by the partners going into the steel mill?

A. We knew that there would be a competition with the other steel mills, and we would have a stronger price.

Q. Stronger price in Portland? A. Yes.

Q. By "stronger," what do you mean?

(Testimony of Manuel Schnitzer.)

A. Higher price. [274]

Q. By what amount?

A. At least the difference in the freight.

Mr. Jones: That's all.

### Recross-Examination

By Mr. Marcussen:

Q. Didn't you testify in the early part of your direct that the price differences were the same as they were with reference to the establishment of this mill? How do you reconcile that testimony with your answer "yes" to counsel's statement that the price was actually increased?

A. I don't get your point.

Q. If you don't understand that, I would like to ask you now to just state in your own words how it was that the establishment of this mill had the effect of raising the price of scrap in Portland?

A. Previous to 1941 or 1942, not counting the O.P.A. which had an area price, the Portland price was \$1.50 a ton to \$2.00 a ton less than the Seattle price. The Bethlehem Steel adjusted the freight costs to the price in Portland and Seattle; and in order to get the scrap in Portland, they must pay the same as the Portland price, which happens to be the Seattle price.

Q. I thought you stated there was a differential of \$1.50 a ton in 1942 between the Seattle and the Portland price? [275]

A. There was.

Q. Now you just stated, if I understand you



(Testimony of Manuel Schnitzer.)

correctly, that now the prices are higher, because, you say, it is,—

A. (Interposing): Not higher than Seattle.

Q. It is the same as Seattle? A. Yes.

Q. Because Columbia Steel is now buying here?

A. Bethlehem Steel is now buying here in competition with the Oregon Steel Rolling Mills. In fact, sometimes they pay more than the local price in order to get it out of here.

Q. They have to pay the same price that is charged to Oregon Steel?

A. The same, and sometimes they pay more.

Q. You set the price on what you charge to Oregon Steel?

A. We don't set the price; we try to get as much as we can; the mills try to pay as little as they can.

Q. Have you given any account as to the difference in price of steel for you as compared with 1942, when you mentioned the differential of \$1.50 to \$2.00 a ton, when Seattle had that advantage over Portland? A. We have a better market.

Q. A much better market? A. Yes. [276]

Q. Is that true all over the country?

A. Yes, it is.

Q. What is the price of steel?

A. As a matter of fact, the market back east is better than it is in Portland.

Q. What is the price of scrap steel that you are talking about?

(Testimony of Manuel Schnitzer.)

A. Number one and two prepared is \$26.00 per gross ton.

Q. I think you testified it was from \$10.00 to \$12.00 a ton back in 1940 and 1942; is that correct?

A. I believe that's right.

Mr. Marcussen: No further questions.

The Court: You may stand aside.

(Witness excused.)

The Court: Call your next witness.

Mr. Jones: I will call Mr. Margosian.

Whereupon,

LEON D. MARGOSIAN

a witness called by and on behalf of the Petitioner, having been first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Jones:

Q. Will you state your name to the reporter?

A. Leon D. Margosian. [277]

Q. What is your occupation, Mr. Margosian?

A. Certified Public Accountant.

Q. How long have you been a Certified Public Accountant?

A. Since 1942; March.

Q. Where did you work in September 1942 up to December 1943?

A. At the Oregon Steel Mills; Oregon Electric Steel Rolling Mills.

Q. You may call it the "Oregon Steel" in your

(Testimony of Leon D. Margosian.)

testimony. You worked for them from September 1942 to December 1943?

A. That's right.

Q. What were your duties there?

A. I was office manager; chief accountant.

Q. After you left there, where did you go to work?

A. Alaska Junk.

Q. How long did you work there?

A. Until September of 1945.

Q. What were your duties at the Alaska Junk?

A. Office manager and chief accountant.

Q. How long have you been engaged in book-keeping or accounting practice?

A. Since 1936.

Q. Are you a graduate of some school of accounting? [278]

A. I graduated from a business school back east, and I also took accounting courses in Northeastern University in Boston, and went for two years to the City College of New York where I studied accounting.

Q. You studied accounting in those schools?

A. Yes.

Q. What company did you work for prior to working for Oregon Steel?

A. Immediately prior to that, I was with the Oregon State Tax Commission, and prior to that I was with Price Waterhouse in Portland.

Q. How long were you with Price Waterhouse?

A. Approximately one and one half years.

Q. What is the business of Price Waterhouse?

A. Certified Public Accountants.

(Testimony of Leon D. Margosian.)

Q. Is that their sole business? A. Yes.

Q. As an employee of Price Waterhouse, did you ever make an audit, an independent audit, of any of the Alaska Junk Company books or any subsidiary of the Alaska Junk Company?

A. Not as an employee of Price Waterhouse.

Q. Did you ever work for any of the subsidiaries of Alaska Junk?

A. Shall I say I worked for an affiliate of the Alaska [279] Junk Company.

Q. Will you explain?

A. In the summer of 1941, during the slack season at Price Waterhouse, I was sent to Alaska Junk Company to make an audit of Plumbing and Heating Sales Company. Based on the findings of my audit, I was placed on the Alaska Junk payroll for approximately ten weeks while I cleaned up the affairs of the company and liquidated it.

Q. During your duties with Oregon Steel, did you ever prepare any vouchers to be paid with R.F.C. funds?

A. Yes; they were all prepared by myself or at my direction.

Q. Did you ever in any of the vouchers that you prepared include charges made by the company against Alaska Junk? A. Yes.

Q. What was the action of the R.F.C. with respect to those charges?

A. Some of them they approved; and some they disapproved.

(Testimony of Leon D. Margosian.)

Q. Were some payments made then?

A. Some payments were made during the period when the mortgage funds were being disbursed.

Q. There has been some testimony about a Mr. McGonigle. Do you know who he was? [280]

A. Mr. McGonigle was the engineer assigned by the R.F.C. to supervise the disbursements of the R.F.C. mortgage funds and to see that the construction of the mill facilities was made in accordance with the standards desired by the R.F.C.

Q. Who was the person that disallowed some of the claims that were made?

A. Mr. McGonigle was what we call the sole arbiter as to any funds that would be disbursed by the R.F.C.; that is so far as I was concerned.

Q. Do you know whether they had any difficulties there while you were there with respect to production?      A. Yes.

Q. Just in a general way, what was the trouble?

Mr. Marcussen: I'll object to that, if your Honor please, on the ground that this witness is not qualified. He is an accountant.

The Court: He may know; I will overrule the objection.

A. Was that question in connection with production?

Q. (By Mr. Jones): Well, what general operating difficulties were there?

A. Well, I think the greatest difficulty in connection with the whole operation was with the con-



(Testimony of Leon D. Margosian.)

struction of the plant, and that was primarily because of the incompetence of [281] the engineers who were employed, in the first place, aggravated by the difficulties to obtain and secure materials during the early stages of the war when every firm was trying to get these materials.

Q. Do you know what the original final estimated cost was?           A. The original?

Q. You had several preliminary surveys, and then you started construction on a final set of figures.

A. The estimate that was used during the construction of the plant was prepared by McKee, and I think that was used by the R.F.C. in disbursing their funds.

(A document was marked Petitioner's Exhibit No. 34 for identification.)

Q. (By Mr. Jones): I am just about to hand you an exhibit, which the Clerk is marking as Petitioner's No. 34. I will ask you if the papers there are in the right order (hands document to witness).

A. Yes.

The Court: If the witness has not stated what the paper is, if there is some way of describing it, it should be in the record.

Q. (By Mr. Jones): This exhibit for identification No. 34, who prepared [282] that?

A. I did.

Q. What is it?

(Testimony of Leon D. Margosian.)

A. It is a memorandum schedule prepared by me showing the actual cost of the plant facilities in comparison with the estimated cost of the plant facilities as taken from the records.

The Court: It shows a comparison of the estimates of what it would cost and what it did actually cost?

The Witness: Yes.

The Court: The Oregon Steel plant?

The Witness: Yes.

Q. (By Mr. Jones): Are these in your handwriting? A. Yes.

Mr. Jones: I will offer this in evidence as Exhibit 34 of the Petitioners.

Mr. Marcussen: I have a question about it, your Honor.

The Court: All right.

Mr. Marcussen: When did you prepare this?

The Witness: That was about the time shown as the date on those schedules, September 23, 1943.

The Court: September 23, 1943?

The Witness: That is right. [283]

Mr. Marcussen: Prepared while you were at the Oregon Steel Mills?

The Witness: Yes.

Mr. Marcussen: When was the last time you saw it?

The Witness: Well, I gave it to the attorney.

Mr. Marcussen: When?

The Witness: Last week.

(Testimony of Leon D. Margosian.)

Mr. Marcussen: In response to his request?

The Witness: No, I volunteered it; I thought it might have some bearing on the case.

Mr. Marcussen: Where did you get it? From what source did you get it?

The Witness: Those schedules were prepared by me at the time when they were considering amending the certificate of necessity.

Mr. Marcussen: Where?

The Witness: In September of 1943.

Mr. Marcussen: Where did you get it when you gave it to counsel?

The Witness: I had it in my possession.

Mr. Marcussen: How did you come to have it in your possession, if this document was prepared for Oregon Steel?

The Witness: When I left Oregon Steel, I took a folder containing my personal papers, and this happened to [284] be in there, entirely without my knowledge.

Mr. Marcussen: Is there a copy of this at Oregon Steel? Was a copy of this submitted and prepared at Oregon Steel?

The Witness: They have a copy of the figures of the original estimate, and, of course, they have figures on the actual cost.

Mr. Marcussen: I am asking you, do they have a copy of this document?

The Witness: No; that is the original and only document.

(Testimony of Leon D. Margosian.)

Mr. Marcussen: Did you prepare this for Oregon Steel in 1943?

The Witness: Yes.

Mr. Marcussen: At whose request for Oregon Steel?

The Witness: At the request of Mr. Wolf and Mr. Schnitzer.

Mr. Marcussen: Is this the very copy that you prepared for them?

The Witness: Yes.

Mr. Marcussen: Did you get this and present this to Oregon Steel, these very papers here?

The Witness: No; they were never presented to them.

Mr. Marcussen: Why not?

The Witness: Because shortly after, they instructed [285] me to prepare a revision of the certificate of necessity,—I will change that. Shortly after they instructed me to prepare a revision of the certificate of necessity, they discarded the idea of revising, and decided to sell the mill without going through the trouble of changing it.

Q. (By Mr. Marcussen): Did you notify them that you had prepared it?

The Witness: They knew I had prepared it.

Mr. Marcussen: They said they were not interested in it, "just keep it"?

The Witness: Well, so far as these particular papers were concerned, I told them I had prepared them, and they said they would not be needed.

(Testimony of Leon D. Margosian.)

Mr. Marcussen: Where have they been all the time?

The Witness: They have been in my personal file.

Mr. Marcussen: Were they folded like that in the personal file (indicating)?

The Witness: Yes.

Mr. Marcussen: By that, I mean these folds here (indicating)?

The Witness: Yes. No, I folded them that way and put them in my pocket when I brought them here to Mr. Jones.

Mr. Marcussen: Did you make any use of them in 1943?

The Witness: I made them just to show the increase over the original estimate; it shows it down to a penny, [286] \$366,000.00.

Q. (By Mr. Jones): I want to ask you a few questions before I continue my offer. The figures on this, where did you get them?

A. They were taken from the ledger of Oregon Steel.

Q. You know they are correct transcriptions of the figures?      A. Yes.

Mr. Jones: I offer this in evidence, your Honor.

The Court: Is there any objection?

Mr. Marcussen: I don't think it is duly authenticated; it is not a document produced in the ordinary course of business. It was not produced by Oregon Steel.



(Testimony of Leon D. Margosian.)

The Court: I will overrule the objection and admit the document in evidence.

(The document heretofore marked Petitioner's Exhibit No. 34 for identification, received in evidence.)

Q. (By Mr. Jones): How much does the exhibit show that the steel mill cost over the estimate?

A. Well, the plant facilities,—

The Court: What do the figures show, the total figures; isn't that the question?

Mr. Jones: I asked him how much the cost of the mill [287] was above the estimate.

The Court: All right.

A. \$366,646.10.

Q. (By Mr. Jones): I am handing you Petitioner's Exhibit 19, and ask you if you prepared that (hands document to witness)?

A. Yes.

Q. Now, I call your attention to the heading on the liability side of this balance sheet called "Advances from Stockholders \$457,825.47," and ask you to explain what enters into that figure?

A. Those represented accounts payable to affiliates.

Mr. Marcussen: Just a minute. The Respondent objects and moves that the answer be stricken on the ground that the balance sheet speaks for itself, because it is termed "Advances by Stockholders."

The Court: Did the witness have anything to do with the preparation of the balance sheet?

(Testimony of Leon D. Margosian.)

The Witness: I prepared it.

The Court: Do you know where the figures came from that went into the balance sheet?

The Witness: Yes.

The Court: I will overrule the objection.

Q. (By Mr. Jones): Will you kindly explain that one item there? [288]

A. Advances from Stockholders represented loans and accounts payable to the affiliates.

Mr. Marcussen: I will object to a characterization of the loans on the ground that it calls for a conclusion of the witness.

The Court: I will overrule the objection.

The Witness: To affiliates and stockholders of Oregon Steel.

Q. (By Mr. Jones): And who were they?

A. Alaska Junk, and Industrial Air, Schnitzer Steel Products, and possibly Central Supply Company; as to the last one, I am not sure.

Q. Why was not that included above under the heading of "Current Liabilities"?

A. Well, it is customary accounting procedure to set aside amounts due stockholders and affiliates, and show them apart from the current liabilities of the concern.

Q. I am handing you Petitioner's 17, and ask you if you recognize what that exhibit is? (Hands document to witness.)

A. That is the open account of the steel mill with the Alaska Junk.

(Testimony of Leon D. Margosian.)

Q. Is that account and the transactions shown in this account, or, rather, the balance shown on this account [289] represented in this figure of \$457,825.47 on the balance sheet? A. Yes.

Q. By the "balance sheet", I mean Exhibit No. 19? A. Yes.

Q. I am handing you Petitioner's 16; what is that?

A. That is the Oregon Steel ledger account with Schnitzer Steel Products Company.

Q. Is the balance shown on Petitioner's 16 as of the date of this balance sheet, as shown in this figure on the balance sheet, \$457,825.47?

The Court: What exhibit is that?

Mr. Jones: On Exhibit 19, the balance sheet.

Q. (By Mr. Jones): Is that figure included in here (indicating)? A. Yes.

Q. Now, when I mentioned a moment ago the balance on Exhibit 17 being included in the figure last mentioned on Exhibit 19, I meant the balance of October 31. Is that the balance that you referred to (indicating)? A. Yes.

Q. I am handing you Petitioner's 19, and I will ask you if you recognize that?

The Court: That is the same one you had before?

Mr. Jones: No, this is Petitioner's 18. [290]

The Court: You said it was Petitioner's 19.

Mr. Jones: I beg your pardon. I meant Petitioner's 18.

(Testimony of Leon D. Margosian.)

Q. (By Mr. Jones): I am handing you Petitioner's 18 and I will ask you if you recognize that?

A. Yes.

Q. What is it?

A. This is the Oregon Steel ledger scrap account with the Alaska Junk Company.

Q. I inquired whether the figure represented by that account on Exhibit 18 is included in the figure of \$457,825.47 on Exhibit 19? A. Yes, sir.

Q. Now then, you mentioned a couple of other companies that may have had balances included in this figure of \$457,825.47 on Exhibit 19. What companies are those? A. Industrial Air Products.

Mr. Marcussen: Just a moment. The Respondent objects to this on the ground that the testimony now being elicited is contrary to the evidence stipulated in the case for the entire balances of Alaska Junk and Morris Schnitzer; it is stipulated in this case.

Mr. Jones: I see no inconsistency; these figures do not add up to that amount; we can add them up. I will [291] withdraw the question.

The Court: Are there any other questions?

Mr. Jones: Yes, your Honor.

Q. (By Mr. Jones): How soon after the end of each month did you ordinarily have the balance sheets out? A. Usually about the 15th.

Q. Now, there is \$190,000.00, roughly, shown on this balance sheet——

The Court: Balance sheet in what exhibit?

(Testimony of Leon D. Margosian.)

Mr. Jones: The balance sheet in Exhibit 19. It is Accounts Payable, \$190,684.06.

Q. (By Mr. Jones): Do you know whether or not any obligations to the Alaska Junk Company or Morris Schnitzer is represented in that figure?

A. There are no obligations shown either to Alaska Junk or Morris Schnitzer represented in this \$190,000.00 on accounts payable.

Q. As shown on Exhibit 19?

A. That is right.

Q. When you were at the Alaska Junk Company as a bookkeeper, did you keep the accounts of the Carlton Coast Liquidators? A. Yes. [292]

Q. And of Central Supply?

A. No, sir. During the first year I was there I supervised the accounting of Central Supply and prepared the monthly financial statement.

Q. My question was, did you keep the account, or did you supervise the account on the Alaska Junk Company's books of Central Supply?

A. Accounts Receivable and Payable, yes.

Q. That would be the same with the Marshfield Bargain House? A. Yes.

Q. And Industrial Air Products? A. Yes.

Q. And what was the Plumbing and Heating Sales Company? Was it operating then?

A. No, sir; that was liquidated in 1941.

Q. You did keep those accounts when you were there? A. Yes.

Q. Did you keep accounts with such concerns



(Testimony of Leon D. Margosian.)

as Max Turn, Munce and Pedrante, Emil Nyberg, P. Pedrante, and Medford Bargain House?

A. Some of the names are familiar; some of the names we didn't have on the books.

Q. At that time? A. At that time. [293]

Mr. Jones: You may cross-examine.

### Cross-Examination

By Mr. Marcussen:

Q. When did you first become a C.P.A.?

A. March, 1942.

Q. Are you a graduate of any college?

Mr. Jones: Before you go on, there is one question I would like to ask.

Mr. Marcussen: All right.

Mr. Jones: What was the difference in the condition of the company's activities between November 1, 1943 and November 26, 1943? Was there much activity? What was the situation there?

The Witness: The mill was completely shut down, and the only section operating was the accounting section preparing the information required for closing the books of the steel company.

Mr. Jones: Would this balance sheet here of Exhibit 19 reflect substantially the condition as it existed on November 26?

The Witness: Yes, sir.

Mr. Jones: That is all.

Q. (By Mr. Marcussen): Are you a graduate of any college? A. No, sir. [294]

Q. I take it you have finished high school?

(Testimony of Leon D. Margosian.)

A. I finished high school; two years of business college; one and one-half years at Northwestern University at Boston; and two years in night accounting courses at the College of the City of New York.

Q. What business college did you attend?

A. Baker College of Worcester, Massachusetts.

Q. Were you a junior or senior accountant at Price Waterhouse?

A. Semi-senior when I left.

Q. You had been a semi-senior for how long?

A. I would say approximately three or four months.

Q. Prior to that, you were a junior?

A. Yes.

Q. What were your duties as junior?

The Court: Counsel ought to know better than to go into details like that; there is too much to be done in the trial on the merits of a case like this.

Mr. Marcussen: Very well, your Honor.

Q. (By Mr. Marcussen): When did you say the mill first began operation?      A. I did not say.

Q. Do you know?

A. The mill began operating progressively, you might say; they started the furnace department some time in June, [295] and they operated that intermittently for several months before they had that going continuously. And then they had the reheating furnace operating; further than that, they

(Testimony of Leon D. Margosian.)

had the roughing rolls; and the second breakdown rolls, and finally the finished rolls.

Q. Can you fix the date approximately when they finally began producing finished steel? Can you fix the date of the functioning of these operations that you mentioned?

A. I would assume the furnace department began operating some time around June; and the rolling mill began operating the latter part of August or the early part of September.

Q. Now, what materials were necessary to operate the rolling mill?

A. Ingots heated to a temperature necessary to produce the plasticity for breaking or reducing the size of the ingots to a finished product size.

Q. When did the furnace start operating?

A. As I stated, I believe the furnace department began operating some time in June.

Q. Where were the ingots heated?

A. In the reheating furnace.

Q. When were they ready for operation?

A. I would say some time in August.

Q. These ingots that you are speaking of—are you speaking of steel ingots? [296] A. Yes.

Q. Where did the mill obtain the steel ingots?

A. They made the ingots.

Q. They made them? A. Yes.

Q. What materials are necessary to make steel ingots?

A. They require scrap; *the* require the ingredients which they mix into the scrap while in the

(Testimony of Leon D. Margosian.)

furnace to produce the necessary chemical composition, including coke and several non-metallic elements.

Q. When was the rolling mill finally ready to start?

A. As I stated, it was some time in August.

Q. Did the mill get all the scrap they needed from sources in Portland or elsewhere?

A. Yes; they had a good supply of scrap and other materials necessary for operation when they were required.

Q. You stated that it is customary in setting up balance sheets to state advances of stockholders separately. Do you know whether that, or the reason for that custom is based on some sound accounting reason?

A. Well, primarily to show creditors and interested people, without looking at a balance sheet what the amount is owing to people who are interested in a particular firm.

Q. Why is it important from an accounting point of view [297] to reveal that information?

A. Well, for one thing, it would more properly reflect your current asset ratio, and for another thing it would appraise any interested people what the amount owing from or to a company is by people interested in that firm.

Q. What effect does it have on the current asset ratio that you are talking about?



(Testimony of Leon D. Margosian.)

A. If it were included in current liabilities, it would increase the current liabilities, of course.

Q. I am merely asking for an explanation of that statement; what effect would it have on the current asset ratio?

A. The effect, of course, would be to increase the current asset ratio of the advances where included in current liabilities.

Q. Can you state how the current asset ratio is computed? Will you state that?

A. Yes; the current asset ratio is the ratio between current assets and your current liabilities.

Q. Were those advances by stockholders, were they current assets?

A. Advances of the stockholders?

Q. No. I beg your pardon. They were a liability. Were they current liabilities?

A. Not in the balance sheet sense of the word; they might be considered so for all practical purposes, however. [298]

Q. And if they were so considered for all practical purposes, you should have listed them, shouldn't you, Mr. Margosian?

A. No, sir.

Q. Why not?

A. Well, as I mentioned before, the customary accounting procedure always, or at least in the accounting textbooks that I have come in contact with, advise that these sums be shown in a separate part of the liability section of the balance sheet.

Q. Yes, and you stated also that it would have



(Testimony of Leon D. Margosian.)

some effect on the current ratio—the current asset ratio? What is that effect, again?

A. I said, if it were included in the current liabilities it would have an effect upon the current asset ratio.

Q. Didn't you say that they were current accounts payable and current liabilities?

A. I said, for all practical purposes.

Q. What do you mean "for all practical purposes"?

A. Well, for practical purposes, you might say, so far as the man on the street is concerned.

Q. And who is the man on the street?

A. The man on the street—for one thing, the owners of the company who wanted to know this, they wanted to know how much the affiliated concerns had due them from the steel [299] mills. If that were included in the current liabilities, that would have been probably hidden and probably overlooked.

Q. Overlooked by whom?

A. By the owners of the firm.

Q. By the owners of the firm?

A. Perhaps "overlooked" is the wrong word.

Q. The owners of what firm?

A. The Oregon Electric Steel Mill.

Q. Who were they? A. Who were they?

Q. They were the stockholders of Alaska Junk?

A. Stockholders of Alaska Junk?

Q. Stockholders of Oregon Steel, but didn't

(Testimony of Leon D. Margosian.)

Alaska Junk have an account on the books showing what was owed by Oregon Steel.

A. That is right.

Q. They didn't depend on the balance sheet to find that out.

A. No, but when the stockholders came in and asked me for a balance sheet, it might be much easier for them to find that figure if I set it apart.

Q. And what justification is there for putting that item down as "Advances By Stockholders," if it is not a current liability? Why wasn't it put down as "Advances by Stockholders" among the "current liabilities"? [300]

A. As a certified public accountant, I approached my balance sheet preparation in connection with what I had been doing, and I think you will find, if you go to any textbook in accounting, that advances are generally shown apart from current liabilities, in a separate section of the liability section of the balance sheet.

Q. If they are current liabilities, what justification is there for excluding them from liabilities, and then stating them separately as advances from stockholders?

A. They could have been placed in there the other way, but this is, I think, the proper way.

Q. Should they not have been placed under current liabilities accounting to good accounting practice?

A. No, sir.

Q. What basis would there be for not placing

(Testimony of Leon D. Margosian.)

them among the current liabilities, if that is what they were?

A. I thought I was following good accounting procedure.

Q. What is the purpose of good accounting procedure?

A. To reflect the financial position at any given time.

Q. That is it exactly. If they are current liabilities, and if they are not listed as such, it will not tell the public accurately just what the situation is?

A. No, sir.

Q. Isn't that correct? [301] A. No, sir.

Q. Why isn't it correct?

A. Anybody who is interested enough in a balance sheet enough to look at it will want to ask questions concerning the various items.

Q. They will want to know how much the stockholders have advanced to the corporation, won't they? A. That is right.

Q. Is there any reason why you should not place that item, also, among the current assets——

A. Current liabilities, you mean?

Q. Yes, that is what I mean; current liabilities. Is there any reason why they should not be placed amongst the current liabilities if they were such?

A. I don't follow your question.

Q. You have the advances from stockholders set below the current liabilities, as a separate item. Could they, or could they not have been listed under

(Testimony of Leon D. Margosian.)

“current liabilities” as “advances from stockholders”?      A. They could have.

Q. And if they were current liabilities, that is where they should have appeared?

A. No, sir. I think we are kind of beating around the bush. As I told you before, I considered them in the nature of current liabilities. I wanted to show a proper segregation [302] on the balance sheet, and so I set it apart.

Q. Mr. Margosian, isn't every one of these items set forth separately under “current liabilities,” so far as the amounts and the characterization there is concerned; aren't they set forth separately?

A. Well, in one sense, that is true; but in my opinion, that would not be under the proper heading.

Q. It would not be under the proper heading if you put them under “current liabilities,” that is, the advances from stockholders; but isn't that exactly what they are, current liabilities?

A. I don't think it would be good accounting procedure, as I told you before.

Q. You think it would be improper, as an accountant?      A. Yes.

Q. Well, I am shocked somewhat at that statement. I know something about accounting, and I never heard of it.

Mr. Jones: I move the court that the remark be stricken.

The Court: It will be stricken. Counsel will confine himself to questions instead of comments.



(Testimony of Leon D. Margosian.)

Q. (By Mr. Marcussen): What is a current liability?

A. A current liability is an amount owing an outsider of the company for amounts which are due and payable within [303] the current year.

Q. Did you say that were due and payable within the current year?

A. Well, at the time the question was indeterminate.

Q. If it was indeterminate, how would they be current liabilities?

A. Because the owners expected them to be paid some time in the future, but I didn't know whether it would or would not be within a year, or what part would be paid within a year, or what part would be longer than a year.

Q. Well, if that is the case, you wouldn't put them under "current liabilities". Is that the reason?

A. Well, if it had been an outside firm, you would determine which part of that amount would be payable within a year and which part of the amount would be included in current liabilities, and the rest would be shown under fixed liabilities.

Q. By "payable within a year," you mean payable by what standard?

A. I don't follow the question.

Q. Who determines whether it is payable within a year?

A. Usually by agreement between the parties.



(Testimony of Leon D. Margosian.)

Q. Did you ascertain what the agreement was between the parties?

A. Well, I had discussed it with them from time to time. [304]

Q. And what did they say?

A. They expected it to be paid as soon as the mill was in operation. That is, periodic payments were to be made against that account after the mill went into operation.

Q. And that is the balance sheet of October 1, 1943?      A. Yes.

Q. And they had barely been in operation?

A. Yes.

Q. And on this balance sheet are items that had been advanced over a period of two years; isn't that true?      A. Yes.

Q. Now, does this current asset ratio have anything to do with the working capital of a corporation?      A. Yes.

Q. What is the working capital of a corporation?

A. The working capital of a corporation is the excess of the current assets over current liabilities.

Q. You mentioned the current asset ratio. What is your experience as an accountant with the current asset ratio of an ordinary manufacturing plant like this usually is?

A. Well, a ratio of two to one, would be desirable; one to one would probably be all right.

Q. One to one would be all right for what kind of an operation?

(Testimony of Leon D. Margosian.)

A. You could get by with it. [305]

Q. That would mean that the current assets—that would mean that your current liabilities that are payable within a year are equal to your current assets?

A. Yes.

Q. You would have no working capital if the ratio were one to one?

A. That is right.

Q. No working capital at all?

A. That is right.

Q. And if these advances to stockholders were included among the current liabilities, you would have an unfavorable current asset ratio, wouldn't you?

A. Yes.

Q. That is to say, the ratio by which current liabilities are less than current assets—by which the current liabilities are greater than the current assets?

A. What do you mean?

Q. That is to say, the ratio by which your current liabilities are greater than your current assets, in that case the ratio would be less than one to one?

A. That's right, if it is so shown.

Q. In other words, an inverse current asset ratio. Now, you mentioned a number of accounts, or a number of accounts were recited to you by counsel for the Petitioners here, including Central Supply, Marshfield Bargain House, [306] Industrial Air Products, M. Turn, Munce and Pedrante, Nyberg, R. Pedrante, and a number of others. You stated that some were on the books and some were not.

(Testimony of Leon D. Margosian.)

A. In other words, we had no account dealing with some of those at the time I was there.

Q. At the time you were there, that was September, 1943 to 1945?

A. No; it was December 1943.

Q. And up to when? To September?

A. September, 1945.

Q. What ones were on the books at the time?

A. Excuse me; that was 1946; September 1946.

Q. You were there then. What was the time? Three years, approximately?

A. I was there in 1944, 1945—about two and one half years.

Q. And what would be the first of those accounts? Do you recall?

A. No, I don't recall the first.

Mr. Marcussen: Do you have it, Counsel?

Mr. Jones: What was that?

Mr. Marcussen: The ones mentioned by the previous witness, Central Supply, and then there was Industrial——

Mr. Jones: Industrial Air?

Mr. Marcussen: There was another one that had some [307] connection with "Industrial".

Mr. Jones: "Industrial Air" is the only one with that name.

Q. (By Mr. Marcussen): Referring to the ones mentioned by counsel, which ones were on the books when you were there and which ones were not?

Mr. Jones: I am going into that in detail with one of the witnesses.

(Testimony of Leon D. Margosian.)

Mr. Marcussen: If your Honor please, that being the case, I will forego cross-examination on that point.

Q. (By Mr. Marcussen): Referring to the accounts shown on the balance sheet, and going back to the question of the accounting textbook which you said it would be advisable to set forth the advances of stockholders separately, that did not say not to put them in the current liabilities, did it, if they actually were current liabilities?

A. It has been a long time since I looked at a textbook, sir, but I think Montgomery's Auditing Practice and Procedure might have something on that.

Q. Could you produce that book in court and show it to the judge?

A. I don't have it with me, but I have it at home.

Q. You do have it at home? [308]

A. Yes.

Q. If this trial goes on tomorrow, which I think it will, will you produce that book?

A. Maybe we can have the attorneys bring it in. I had hoped I would not have to be here tomorrow. I am supposed to be in Salem.

Q. I would like to interrogate you about that. I want to be sure that we understand you on that point. Will you kindly produce it?

A. You wish me to be here tomorrow?

Q. Yes, indeed, for further cross-examination on that point.

(Testimony of Leon D. Margosian.)

Mr. Jones: Perhaps you would do it tonight; perhaps he would come back after he leaves the stand, so that he can go home this evening.

Mr. Marcussen: I have no objection to that; if he comes tonight, that would be quite satisfactory. I have no further questions of the witness.

The Court: Does the Petitioner have any questions?

Mr. Jones: Only this; I would like to offer the tax return, because I think the witness has prepared one, and we might use him to put that in.

### Redirect Examination

By Mr. Jones:

Q. Did you prepare the 1943 return for Alaska Junk? [309]

A. I prepared the 1943 return, yes.

Mr. Jones: May we have the returns for 1943 and 1942?

Mr. Marcussen: For whom?

Mr. Jones: For Alaska. I served notice on you for the years 1943 and 1942, for the Alaska partnership return.

The Court: I think we might take a little recess while they are searching.

(Recess.)

Mr. Jones: I should like to offer in evidence the 1942 and 1943 tax returns as our next exhibit.

The Court: Are you making them a single exhibit? Or two exhibits?



(Testimony of Leon D. Margosian.)

Mr. Jones: Separate exhibits.

The Court: No. 35 is the partnership return for what year?

Mr. Jones: Petitioner's 35 would be the 1942 tax return; and Petitioner's 36 would be the 1943 return. I offer them in evidence.

The Court: Is there any objection?

Mr. Marcussen: No objection.

The Court: They will be received and so marked.

(The documents above-referred to were received in evidence and marked as Petitioner's Exhibit No. 35 and No. 36.) [310]

Mr. Jones: Are these the returns or copies?

Mr. Marcussen: They are the original returns.

Q. (By Mr. Jones): Are you employed by the Alaska Junk Company now?

A. No, sir; I am practicing for myself, in Salem, Oregon.

Q. How long have you been there?

A. One and one-half years.

Q. I would like to ask you also about one item on Exhibit 17. There is an entry of March 31, 1943, which reads, "to record debentures 11/30/42." Is that your handwriting? Did you make that record?

A. No; that was made by our bookkeeper.

Q. Under whose supervision?

A. Under my supervision.

Q. What does that "11/30/42" indicate?

(Testimony of Leon D. Margosian.)

A. At the time it referred to the date on which the debentures were issued, and I made this notation on the journal to that effect.

Q. Had you seen the debentures at the time it was recorded, personally, the physical debentures?

A. No.

Q. About when would the November balance sheet have been available?

A. I did not prepare—we did not prepare the November balance sheet.

Q. There was a November balance sheet—  
The Court: Of what year?

Mr. Jones: 1943.

The Witness: Of 1942, do you mean?

Q. (By Mr. Jones): That entry was made in 1943, was it not (hands document to witness); but this was November 1942 down there (indicating). The entry shows it was made March 31, 1943, but on the entry it reads, “to record debentures issued 11/30/42.” And my question is, what does that 11/30/42 mean?

A. In the light of my knowledge at the time of the entry or at the present time?

Q. No; at the time of the entry.

A. At the time of the entry I thought the debentures had been actually issued as of that date.

Q. Had you ever seen the debentures?

A. No, sir.

Q. I mean, at the time of the entry.

A. No.

(Testimony of Leon D. Margosian.)

Q. Or at the time the entry was made, you said it was not made by you personally?

A. That is right.

Q. Now, do you know whether there was a balance sheet made for 11/30/42? [312]

A. No, sir.

Q. Was there or was there not?

A. There was not.

Q. So, whether or not that is the correct date of the debentures, at least you thought it was at the time you had the entry recorded? A. Yes.

Mr. Jones: That's all.

The Court: Are there any further questions by the respondents?

Mr. Marcussen: Yes; just a question or two.

Recross Examination

By Mr. Marcussen:

Q. You have just discussed this entry that you were examined about, Mr. Margosian, of November 30, 1942. Was that incorrect?

A. The date the debentures were issued was different from that November 30 date.

Q. So the November 30, 1942 date is incorrect; is that right? A. Yes.

Q. Do you know when the debentures were issued? A. I talked to——

Q. (Interposing) Do you know?

A. I do not know the exact date; no, sir. [313]

The Court: Does the stipulation show it?

Mr. Jones: The stipulation shows the date.

(Testimony of Leon D. Margosian.)

Mr. Marcussen: I have no further questions.

The Court: You may stand aside.

(Witness excused.)

The Court: Call your next witness.

Mr. Jones: I will call Mr. M. R. Schnitzer.

**M. R. SCHNITZER**

a witness called by and on behalf of the Petitioners,  
having been first duly sworn, testified as follows:

**Direct Examination**

By Mr. Jones:

Q. Will you state your name?

A. M. R. Schnitzer.

Q. What is your occupation, Mr. Schnitzer?

A. Public accountant.

Q. Are you a graduate of any school?

A. Yes, sir; the University of Oregon.

Q. Did you study accounting there?

A. Yes, sir.

Q. When did you first start in doing accounting  
work or bookkeeping work? A. In 1931.

Q. Were you ever employed by the Alaska Junk  
Company? [314] A. Yes.

Q. When?

A. In approximately June of 1934 to July of  
1944; approximately ten years.

Q. What were your duties?

A. I was the chief accountant, credit manager,  
assistant office manager, and then office manager.

(Testimony of M. R. Schnitzer.)

Q. What were your duties between the time you started to work until December 1943?

A. I was accountant for the firm.

Q. And from that date until you left in 1944?

A. Pardon me; I didn't get the date.

Q. From December 1943 until you quit?

A. What is the question?

Q. Just a minute. Explain in your own words the periods of your various jobs.

A. From 1934 until March of 1943, I was accountant and then this other work overlapped. And then in March of 1943 I became office manager, and included in that work of accounting work, until December of 1943, until Mr. Margosian came in; and I worked with him, or he worked with me until July of 1944 when I left.

Q. From March of 1943 until you left, you were office manager?

A. Yes; and in charge of accounts. [315]

\* \* \*

Q. During the time that you were keeping books at the Alaska Junk Company, did you handle the accounts—did you handle all the subsidiary accounts of the Alaska Junk Company?

A. Yes.

(A document was marked as Petitioner's Exhibit No. 41 for identification.)

Q. (By Mr. Jones): I am handing you Petitioner's 41 for identification, and ask you to state what that is (hands document to witness)?



(Testimony of M. R. Schnitzer.)

A. Have you got that other page?

Q. Where is that other page?

A. Here it is (indicating). Do you want to put it in here (indicating)?

Q. Yes, if it is a part of the same account.

A. Yes.

Q. All right.

The Court: How many sheets are there.

The Witness: Forty-nine pages.

The Court: Forty-nine pages? [320]

The Witness: Total pages; that is the original records of the Alaska Junk Company accounts receivable with the National Machinery Company of Eugene.

Q. (By Mr. Jones): Did you put the entries on there? A. No, sir.

Q. Was it kept under your supervision?

A. No, sir.

Q. Were you working for them at the time?

A. No, sir.

Q. I guess you don't know anything about it?

A. Yes, I do.

Q. All right.

A. This account was wound up in 1933; that is why I said it was not under my supervision. But, in later years, I worked on the write-off, and I regularly found it necessary to work with them.

Q. You familiarized yourself with those accounts? A. Yes.

Q. What is this?

(Testimony of M. R. Schnitzer.)

A. It is the record of the merchandise and cash advances to the National Machinery Company of Eugene, which was a subsidiary corporation of the Alaska Junk Company, for the period of January 1, 1928 until December 31, 1933, when it was written off and closed. [321]

Q. What do you mean by written off and closed?

A. This corporation was liquidated by the Alaska Junk Company in the years 1932 and 1933. It resulted in a bad debt to the Alaska Junk Company, which was written off.

Mr. Marcussen: I'll object to that as having no materiality to the issue here. That is a bad debt that they took back in 1933.

The Court: Is it one of those collateral companies that we have been talking about?

Mr. Jones. Yes.

The Court: It is a sort of a back history?

Mr. Jones: Yes.

The Court: I will overrule the objection. Go ahead.

The Witness: Where was I?

Q. (By Mr. Jones): Are you familiar with the various items in the account?

A. Yes; there was merchandise and cash advances, less cash received and merchandise received, and, of course, the final write-off.

The Court: What is the necessity of having this exhibit in detail? It seems to me it would suffice if you stated that would be a record of that account.

(Testimony of M. R. Schnitzer.)

Mr. Jones: Very well. I will have the exhibit at hand, and not offer it in evidence, but just let him testify [322] from it.

The Court: It seems to me you have enough pertinent exhibits without going into so much detail.

Mr. Jones: This document has been identified as Exhibit No. 41 for identification. We can just call it the account if we are not going to put it in evidence, if you think it will clutter up the record.

Mr. Marcussen: I think it will facilitate matters in handling the case if the document is given a number.

The Court: If you interrogate the witness about it, it should have a number for identification.

Mr. Jones: I think it has already been identified.

The Court: If you are not going to interrogate him, that is another thing.

Mr. Marcussen: I am going to interrogate him on cross-examination.

Q. (By Mr. Jones): I will hand you another exhibit which I will have marked Petitioner's Exhibit 42 for identification. Will you explain that, please?

A. That is the accounts receivable of the Central Supply Company. The original record of the Alaska Junk Company against the Central Supply Company from the opening of the Central Supply Company until there appears to be a current date,

(Testimony of M. R. Schnitzer.)

and included the various advances for cash and merchandise, less the stock taken by Alaska Junk.

Q. Did you supervise the keeping of that record? A. Yes.

Q. You are familiar with the categories of the items? A. Yes.

Q. And you have summarized them in your previous statement? A. Yes.

The Court: What do you mean by "your previous statement"?

Mr. Jones: His answer just immediately preceding.

Q. (By Mr. Jones): Do you know the nature of the cash advances that are shown on that record.

A. Yes.

Q. Will you explain them a little more fully?

A. The cash advances seem to include the payroll, cash advances to the company for its own distribution, rent. No, the rent was not a cash advance. I think that covers it.

Q. That is the nature of these cash advances?

A. Yes.

Q. Were those advances paid back? Does that account show?

A. Yes. The Alaska Junk Company, individuals owning the Alaska Junk Company, paid for stock to the extent of [324] \$70,000.00, \$50,000.00 of which was posted against the account, and later the balance was paid out of the operating profit of the Central Supply from time to time, and subsequently

(Testimony of M. R. Schnitzer.)

became a current monthly account; that is to say, they paid it, or paid off every month.

Q. Do you know whether that company was handled on the books of the Alaska Junk Company in the same manner that the Oregon Electric Steel was handled?

Mr. Marcussen: If your Honor please, I'll object to that on the ground that it calls for a conclusion of the witness; the record will speak for itself; and the documents are in this courtroom.

The Court: I know, but the Court does not want to examine all the documents.

Q. (By Mr. Jones): Do you know whether the accounts were handled in the same manner as Oregon Steel?

A. The books were handled exactly the same.

Q. With respect to the accounts receivable and the cash advances? A. Yes, sir.

Q. And the payment of stock in the company? I mean, stock in the Central Supply? A. Yes.

Q. That was subscribed by the partners of Alaska Junk? [325]

A. Yes; did I give you the figure of \$70,000.00?

Q. Yes.

A. I think the figure was \$50,000.00 for the stock subscription.

Mr. Marcussen: And that was offset against this account?

The Witness: Yes.

Q. (By Mr. Jones): Now, I am handing you



(Testimony of M. R. Schnitzer.)

for your inspection another document which has been marked by the Court as Petitioner's 44, and I will ask you to state what that is?

A. That is the original record of the Alaska Junk Company Accounts Receivable with the Carlton and Coast venture.

Q. Was that kept under your direction and supervision? A. Yes.

The Court: Covering what period of time?

The Witness: Well, from October of 1941 until I left, which was in—no, I turned it over to Mr. Margosian in 1943.

Q. (By Mr. Jones): What was the nature of the entries on that account?

A. Merchandise sold by the venture and furnished to it, and cash advances to it.

Q. Did the Carlton and Coast Liquidators keep a separate set of books? [326]

A. Yes; they had a separate set of books and a joint venture between the Alaska Junk and Dulien Steel Products.

Q. That was kept as a separate record?

A. Yes; I kept those, too.

Q. And did you keep this as a separate record on the Alaska books, too? A. Yes.

Q. What was the nature of the cash advances on this account?

A. Checks drawn to the order of Carlton Coast Liquidators for their use and distribution in their operations.

(Testimony of M. R. Schnitzer.)

Q. And how were those repaid?

A. When I left, they had not been repaid. If I might look at the record, I might be able to give you an answer.

Q. All right. (Hands document to witness.)

A. It appears that the offsetting entries in this investment in the Carlton Coast Liquidators—it appears that the remainder there was paid by the Carlton Coast Liquidators by checks.

Q. I believe you covered this. I neglected to ask you a question about Exhibit 42, or what it covers?

A. Will you repeat that?

Q. I neglected to ask you what the account, Exhibit 42, covers?

A. I answered that; it was from 1940 until the current [327] date, now.

Q. Handing you Petitioner's 45 for identification, I will ask you what that is?

A. That is the original record of the Alaska Junk Accounts Receivable of the account of Marshfield Bargain House at Marshfield, Oregon.

Q. What are the categories of the items there?

A. Primarily merchandise sold to it, but it includes some cash advances given to it.

Q. What is the nature of the cash advances?

A. They were advances on purchases of scrap iron which they purchased.

The Court: What period does it cover?

(Testimony of M. R. Schnitzer.)

The Witness: It starts in 1931 until the last time they did business, September 11, 1947.

Q. (By Mr. Jones): I hand you Petitioner's Exhibit 46 for identification, and I will ask you to state what that is?

A. That is a part of the record of the Alaska Junk Company Accounts Receivable against the Vaughan Motor Works during the period May 4, 1928, to October 18, 1930.

Q. What is the nature of the items on it?

Mr. Marcussen: I will object to it on the ground that it is entirely too remote.

The Court: I will sustain that objection. That is entirely [328] too far away in point of time.

Q. (By Mr. Jones): I hand you here Petitioner's 49 for identification, and ask you to state what that is?

A. That is an account carried through the Alaska Junk Accounts Receivable, which was opened in 1937 in order to keep tab of the cash advances to various small junk dealers.

Q. When was the account closed?

A. It was closed February 26, 1945.

Q. And what was the nature of the advances?

A. It is practically all small cash advances to small dealers for scrap iron.

Q. For what purpose?

A. For scrap iron which they wanted to purchase and sell to the Alaska Junk.

Q. Was the money given by the Alaska Junk

(Testimony of M. R. Schnitzer.)

to the small dealers for the purpose of purchasing merchandise for them?

A. In some instances they might have purchased merchandise for the Alaska Junk, but in other instances they may have purchased for themselves, and were unable to complete the payment or the wrecking or the preparation of it.

Mr. Marcussen: Now, if your Honor please, there has been a sufficient showing to indicate that this one in particular, as well as most of the others, pertain for the most part, as has already been revealed on the cross-examination [329] of the preceding witnesses, to advances which were made to small junk dealers or small collectors of scrap iron for the purpose of securing scrap iron which this company, The Alaska Junk Company, was in the business of selling to the steel mills or various sources of supply. An attempt is made to demonstrate that this company was in the business of making loans and advances to other organizations, just as the petitioners contend the loans were made to Oregon Steel in this case. I think it is clear from what already had been shown that these advances were made for the purpose of getting this scrap steel collected.

The Court: That is a matter the Court will have to decide in order to determine the effect of it. What we are getting is the facts, and you can argue the effect of it later.



(Testimony of M. R. Schnitzer.)

Mr. Marcussen: May it be noted that counsel for the respondent has an objection.

The Court: Yes, counsel for the Respondent objects and an exception is noted. I will ask counsel to restrict it for the purpose of showing the business in which the petitioners were engaged.

Q. (By Mr. Jones): Do you know whether its course of conduct, as shown by this Petitioner's 49 for identification here, was carried on during the entire time that you worked there? [330]

A. Yes.

Q. I now hand you Petitioner's 46 for identification, which it was ruled to be at too early a date,— I don't believe I had made a showing exactly as to the date at that time; the date on there is November 30, isn't it?

A. 1930, you mean?

Q. Yes, I mean 1930.

A. Yes.

Q. You went there in 1933?

A. 1934.

Q. At that time, that is, at the time that you were there, were they carrying on in the same way?

A. Yes.

Mr. Jones: Your Honor, I would like to put this account in for the simple reason it shows a continuous course of conduct from the inception of business through the years in question.

The Court: An objection has been sustained on that account, from 1928 to 1931, I understand?

Mr. Jones: This is the account from 1928 to 1930.



(Testimony of M. R. Schnitzer.)

The Court: That is pretty far back. Let us confine it to transactions a little closer.

Q. (By Mr. Jones): Now, I am handing you Petitioner's identification No. 48, and ask you to state what that is? (Hands document [331] to witness.)

A. These are the ledger sheets from the accounts receivable ledger of Alaska Junk Company, covering the account of M. Turn, LaGrande, Oregon, from November 2, 1928, until April 30, 1945.

Q. Will you tell us what the items on the account are?

A. Principally it covers merchandise sold to it, but it includes some cash advances, also, to Mr. Turn. I see here a couple of credits for scrap iron received.

Q. Does it show how those cash advances were paid?      A. By check.

Mr. Marcussen: What was the answer to the question?

The Witness: By check.

Q. (By Mr. Jones): How was it repaid?

A. Repaid in merchandise and scrap iron.

Q. I am handing you Petitioner's 47 for identification, and I will ask you what that is? (Hands document to witness.)

A. These are the original ledger sheets of the accounts receivable of the Alaska Junk Company's books of account showing the account with the Industrial Air Products Company from December

(Testimony of M. R. Schnitzer.)

6, 1940, to and including December 17, 1943. [332]

Q. Does it show any cash advances?

A. Yes.

Q. What are the categories? Are there any other categories than the cash advances?

A. Merchandise and advances to Industrial Air Products.

Q. How were the advances repaid?

A. First by offset for the stock purchase of the partners of the Alaska Junk, and then later on by payments by check of the Industrial Air Products.

Q. I hand you herewith Petitioner's 50 for identification, and ask you what that is?

A. These are the original ledger sheets on the accounts receivable ledger of the Alaska Junk for the account originally of Munce and Pedrante, and later assumed by William Munce, one of the parties named there, and his son.

The Court: For what period?

The Witness: The period starts in 1940 and winds up in September, 1943.

Q. (By Mr. Jones): What was the nature of the items on it?

A. Cash, merchandise and supply.

Q. You speak of cash; you mean cash advances?

A. Cash advances directly to them, and cash advances on their behalf.

Q. By Alaska Junk? [33]

A. By Alaska Junk.

Q. And how was it repaid?

(Testimony of M. R. Schnitzer.)

A. It was repaid in part by cash when a check was given back to Alaska Junk, which they had given for work done. And later, during the end of the account, they turned over to Industrial Air Products, another subsidiary of Alaska Junk, a truck which was valued at \$5,000.00, and we, in turn, charged Industrial Air Products and credited William Munce with \$5,000.00.

Mr. Marcussen: You credited Munce?

The Witness: We credited Munce and charged the Industrial Air.

Q. (By Mr. Jones): You stated the period of time, I believe? A. Yes.

Q. Handing you Petitioner's 51, for identification, I will ask you to state what that is? (Hands document to witness.)

A. This is the original ledger sheet of the Alaska Junk from its accounts receivable ledger against Emil Nyberg.

Q. What does it show?

A. It covers the account from the period of June, 1937, until December of 1937 for cash advances directly to Mr. Nyberg, and cash advances on his behalf, plus a small amount of merchandise. [334]

Q. Does it show how the repayments were made?

A. This was transferred out from this account to a separate venture account which we carried. In this case, if I might add, Nyberg gave up the job, and we cancelled out the advances he had gotten against the total cost of the job.

(Testimony of M. R. Schnitzer.)

Q. Were those advances made before you had received any merchandise from him?      A. Yes.

Q. In any of the other accounts, were advances made before you received any merchandise from the person to whom the advances were made?

A. Invariably.

Q. I am handing you for your inspection, Petitioner's 52 for identification, and ask you what that is? (Hands document to witness.)

A. These are the original ledger sheets of the accounts receivable account of the Alaska Junk Company with R. Pedrante.

The Court: Covering what period?

The Witness: August 12, 1938, until December 31, 1940.

Q. (By Mr. Jones): What items do they show?

A. Principally cash advances to Mr. Pedrante, and for merchandise supplied to him.

Q. And how were they repaid? [335]

A. They were repaid in cash for the work he did; in other words, we gave him a check for the work he had done down to the final part, and then it was written off. We gave him a credit for the work he had done, and the balance was written off.

Q. I am handing you for inspection Petitioner's 53 for identification, and ask you to state what that is and what period of time it covers, and what items are on it?

A. These are the original ledger sheets of Alaska Junk from its accounts receivable ledger for the



(Testimony of M. R. Schnitzer.)

account of Medford Bargain House, Medford, Oregon, during the period July 3, 1934, until February 12, 1948. It covers merchandise sold to them plus cash advances to them.

Q. And how were the cash advances repaid?

A. The cash advances were repaid in scrap iron.

Q. Were there any advances made to them before the merchandise was received? Before they had any merchandise to deliver to Alaska?

A. Several times.

Q. And when there was a debit balance on the books when the advances were made? A. Yes.

Q. In other words, they were indebted to the Alaska Junk when some of the advances were made?

A. Most times. [336]

Q. Did that ever exist with respect to any of the other accounts we have been talking about?

Mr. Marcussen: I'll object to that; that is far too general a question.

The Court: I will overrule the objection.

A. Yes.

Q. (By Mr. Jones): I am handing you now for your inspection what the Clerk has marked as Petitioner's Exhibit 54, and ask you to state what period of time it covers, and what items appear on it?

A. This is the ledger sheet of the Alaska Junk Company from its accounts receivable ledger labeled "Special Account Steel Tank and Pipe Company."

The Court: For what period?



(Testimony of M. R. Schnitzer.)

The Witness: February 16, 1934; at which time the Alaska Junk Company gave a \$100,000.00 cash advance to that company, until May 10, 1935, at which time the account was paid up in full contra credit for scrap iron.

Mr. Marcussen: I'll object to that, if your Honor please, on the ground that it is too remote.

The Court: I think I will sustain that. I think we have enough of the others.

Mr. Jones: Very well. [337]

Q. (By Mr. Jones): We have one here, Petitioner's 55 for identification, which I will ask you what that is? (Hands document to witness.)

A. These are the original ledger sheets of the Alaska Junk Company account receivable ledger for the account of Plumbing and Heating Sales Company.

The Court: For what period?

The Witness: From January 22, 1940, until February 3, 1942.

Q. (By Mr. Jones): What does it cover?

A. It covers merchandise supplied to that company, plus cash advances to that company. It reflects offsetting entries for stock which the Alaska Junk Company had subscribed, and it reflects later the liquidation of the company.

Q. Was that account handled on the books of Alaska Junk the same as Oregon Steel?

Mr. Marcussen: I'll object to that; that is leading.

(Testimony of M. R. Schnitzer.)

Q. (By Mr. Jones): How was that account handled on the books of Alaska Junk as compared with Oregon Steel? A. Identically the same.

Q. And the cash advances consist of what items?

A. Let me see the account.

Q. Surely. (Hands document to witness.)

A. The cash advances to it consists of cash advances [338] directly to the corporation for distribution by itself; cash advances on its behalf to employees of that company; and cash advances apparently for licenses and miscellaneous small items.

Q. How were they repaid?

A. First, there was \$200,000.00 stock subscription which was offset against the account, and later we liquidated the company and took over the proceeds of the assets, accounts receivable, and so on.

Q. Now, then, are you acquainted with this account, Exhibit 26? (Hands document to witness.)

A. Yes.

Q. Now, there has been testimony in here, and we don't want to repeat it, that there were cash advances in there from Alaska Junk to the Oregon Steel. How was the money secured by Alaska that went to make up those advances?

A. There were three sources; cash which the Alaska Junk obtained from its regular operation of business, that is, sales, which normally would have been returned to the bank for the repayment of obligations; new loans made by the Alaska Junk from the bank; and loans made by individuals.

(Testimony of M. R. Schnitzer.)

Q. What was the nature of the bank loans that Alaska made in order to procure the money?

A. They are all straight ninety day notes.

Q. And what interest rate did they pay?

A. I believe six per cent at the time. [339]

Q. Was that the current rate?

Mr. Marcussen: What is the purpose of this?

Mr. Jones: To show credit,—to show the credit was so extended that they didn't have a cash position to enable them to invest large sums in the company.

Mr. Marcussen: I'll object to that.

The Court: I will overrule the objection. Proceed.

Q. (By Mr. Jones): What interest rate was Alaska Junk paying to the bank?

A. I believe six per cent at that time.

Q. Why were they paying six per cent?

Mr. Marcussen: I'll object to that as calling for a conclusion.

Q. (By Mr. Jones): Do you know why?

A. Yes.

Q. Did you go to the bank and talk to them about it? A. Yes.

Q. Why were they paying six per cent?

A. Because at no time did they pay off the notes in time in the six years; and they had an agreement with the bank when they paid off, they would renegotiate the rate.

(Testimony of M. R. Schnitzer.)

Q. What amount of money did the Alaska Junk ordinarily [340] have as cash on hand and in the bank?

A. Some figure less than \$10,000.00; some figure between three and eight thousand dollars.

Q. Was there any time in the month when they had a larger cash on hand position?

A. Yes; around the tenth of the month, when they made collections; and we held quite an amount until we found out what we had to pay out; if there was a deficit, we borrowed more money from the bank, or if there was a surplus, we turned it over to the bank.

Q. And during the rest of the time your cash position was from three to eight thousand dollars in the bank?

A. That is correct.

Q. Now then, the bills that you paid for the Oregon Steel and charged on the account of Oregon Steel, on Alaska's books, referring to Exhibit 26, how would you secure money to make those payments?

A. Well, if we didn't have it we would go to the bank and borrow.

Q. On the ninety-day note terms?

A. Yes.

Q. Now, did you ever form a judgment while you were an accountant there of the amount of money that the Alaska Junk Company could afford, under its own capital structure, to invest in Oregon Steel? [341]

Mr. Marcussen: I'll object to that on the ground



(Testimony of M. R. Schnitzer.)

that it calls for a conclusion, and it is wholly immaterial, besides, what they could afford.

Mr. Jones: If the Court please, one witness has testified that this accountant had figured about how much the Alaska Junk could afford to invest.

The Court: I think the opinion of this witness would be admissible.

Mr. Marcussen: If your Honor please, what we are interested in, it seems to me, is getting the facts. That is the only thing that can determine the tax liability of the petitioners.

The Court: He can state what his opinion is of what could be done, and you can cross-examine to see what it is based on. I think it is admissible. I will overrule the objection.

Q. (By Mr. Jones): Did you ever, while you were working there, and during the time that they were interested in the Oregon Steel, make a study and come to any conclusion as to what Alaska Junk could afford to invest in the capital stock of Oregon Steel?     A. Yes.

Q. And how much did you conclude?

A. It actually came about through the discussions. [342] We were agreed that the Alaska Junk could afford some \$62,500.00, and later, again, the question came up as to whether we could afford \$125,000.00 rather than \$62,500.00; and I suggested that if they went beyond that,—

The Court: Beyond what?

The Witness: Beyond \$125,000.00, and tying it



(Testimony of M. R. Schnitzer.)

up in a non-liquid form, that that might jeopardize the credit of Alaska Junk, and thereby their own safety.

Q. (By Mr. Jones): What was their credit position?      A. At which time? [343]

Q. At the time they went to \$125,000.

A. They owed the bank between \$200,000 and \$225,000. They owed to private individuals another sum, but I don't recall exactly what it was. I think it was between \$35,000 and \$40,000. And at the same time they had previously invested money in Industrial Air Products and Central Supply, which investments, together with the accounts receivable which were then in liquid condition totaled approximately \$170,000 or \$180,000. So right at that moment it was my impression that they were pretty much squeezed right then.

Q. There is one question I would like to clear up. There has been some mention in the pleadings with respect to Schnitzer and Wolf Machinery Company. Can you tell us what that is?

A. That is another assumed name for the Alaska Junk. It is just another name to use. It appears that certain individuals dislike the name "Junk."

Q. On Exhibit 26, can you give us the types or categories of the items on it?

A. Yes. Four categories; the first category is merchandise sold to the mill from the stock of Alaska Junk Company; there is merchandise ordered by the Alaska Junk for the mill, without

(Testimony of M. R. Schnitzer.)

profit and billed to them at cost; there are cash advances to the mill for their own distribution; and then there is cash advanced on behalf of the mill at their request. [344]

Q. To pay a third party?

A. To pay other parties.

Q. What was the balance on that account that you have there on August 31, 1942?

The Court: Account in what exhibit?

Mr. Jones: This is on Exhibit 26.

A. Approximately \$285,000 billed already, with other bills going through to make it approximately \$299,000.

Mr. Marcussen: What was that date, again?

The Witness: October 31, 1942.

Q. (By Mr. Jones): Also, will you give me the balance on the account on Exhibit 26 on November 30, 1942?

A. November 30, approximately \$301,000.

Q. That is, due from Oregon Steel to Alaska Junk?

A. Yes.

Q. Now then, do you know anything about the transactions that led up to the issuance of the debentures? What was the reason for the debentures?

A. It is my recollection that the Alaska Junk had subscribed originally about \$62,500 in stock and changed it in, I believe, December of 1942 to \$125,000, which would have left,—which, when an entry was made to offset the \$125,000, it would have left

(Testimony of M. R. Schnitzer.)

a balance of \$174,000 as shown by the books then; and in their negotiations with the RFC which resulted, [345] as I remember, in a standby agreement whereby the Alaska Junk would not get paid for this balance. Alaska Junk wanted interest on this balance, because it was paying interest, so during the discussion it was suggested that Alaska Junk and Morris Schnitzer both take debentures to cover the balance of the stock beyond the stock purchase on that date.

Q. I notice that you made credits on that account in July. How was it that it took from December until July until there was a credit on the account?

A. Well, the attorney who issued the debentures and the stock certificates at that time was Mr. John Reilly; he was very busy and hard to pin down, and after he got his instructions we just waited; finally, after a few months, not knowing whether the certificates were issued. I called him up and asked him how it was, not having information prior to thereto, and he told me that they had been issued; and therefore I made the entries as soon as I had knowledge of their being issued.

Q. Now, did you have in your capacity as a bookkeeper there at the Alaska Junk Company a binding guarantee by Morris Schnitzer?

A. Yes.

Q. There is almost a concluding entry here on Exhibit 26 (indicating). First I would like to show

(Testimony of M. R. Schnitzer.)

you the journal entries on Exhibit 6, and I will ask you in whose handwriting [346] the journal entries on Exhibit 6 is?           A. Mine.

Q. Now, the journal entries, are they all in your handwriting on all pages?

A. I am just checking it (indicating). All of these pages, yes.

Q. Now, I call your attention particularly to the last journal entry on page J-23 and ask you where you got the information to prepare that journal entry?

Mr. Marcussen: Which journal entry?

Mr. Jones: The last one.

The Court: What was the amount, to identify it?

The Witness: \$83,581.20.

Q. (By Mr. Jones): Will you answer the question?

A. This entry charges the Schnitzer Steel Products, or Morris Schnitzer. I considered, after making my computations of his guarantee of one-third as against the two-thirds of Alaska Junk, that would be the figures. The figures consisted of two parts; the accounts of the Alaska Junk of Schnitzer Steel Products. The figures on Alaska Junk I had, and the figures on Schnitzer Steel I seem to remember getting from Mr. Margosian. He was working at the steel mill and had set up a Schnitzer Steel Products credit to his account.

Q. What was the basis of that charge of \$83,-



(Testimony of M. R. Schnitzer.)

000? What [347] warranted the charge to Morris Schnitzer of that \$83,000?

A. That was charged to Schnitzer Steel Products and credited to Oregon Steel.

Q. Will you explain it?

A. He guaranteed to the partners of Alaska Junk that if there were any losses, he would bear his proportionate share, that is, his one-third full share of any losses in Oregon Steel, if any. Now, the total loss exclusive of the stock, was agreed upon and these were the resulting figures.

Q. I don't care to have you tell us how you got the figure, but all I want to know is whether the last journal entry was computed on the guarantee?

A. Yes.

Q. The guarantee of Morris Schnitzer to the Alaska Junk? A. Yes.

Q. Who made the write-off on this account of the bad debt? A. I did.

Q. What business was the Alaska Junk Company engaged in during the time that you were there?

Mr. Marcussen: If Your Honor please, I object to that on the ground that it is stipulated in the record.

The Court: I think that is already stipulated.

Mr. Jones: If Your Honor please, we have an agreement [348] that a part of the business was stipulated, but I expressly brought it up with the



(Testimony of M. R. Schnitzer.)

understanding I had that I could bring up any evidence which is not inconsistent with that.

The Court: What is the purpose?

Mr. Jones: I want to show by this witness that our loss, that is, this bad debt loss, was a normal business bad debt, incurred in a normal business operation.

Mr. Marcussen: I do have that understanding with counsel. If Your Honor please, my objection is not inconsistent with my understanding with counsel, and is not any back-tracking, and to that extent my objection is on the ground that it calls for a conclusion; whether or not the company was engaged in the business that counsel contends is something for the Court to decide.

The Court: The question, as I recall it, is what business the company was engaged in. That would be a matter of fact. If the stipulation covers it, I don't care to waste any time; but if this is anything that is required to be brought out, go ahead.

Mr. Jones: The stipulation is all right as far as it goes, but it is incomplete.

Mr. Marcussen: He wants to get this to show that the company invested money in various enterprises; he wants to bring in evidence that Your Honor has to decide. It won't perhaps impeach the stipulation, but I do object to it, and I [329] honestly state to Your Honor that it simply calls for a conclusion which it will be Your Honor's function to decide.

(Testimony of M. R. Schnitzer.)

The Court: If it is a fact, that is one thing. If you are practicing law, that is not a conclusion; that is a fact; I will overrule the objection.

Mr. Jones: Do you know what business enterprises the Alaska Junk Company was engaged in while you were with them?

The Witness: You are using the plural there?

Q. (By Mr. Jones): Yes.

A. Well, it was in the pipe business, it was in the plumbing business; it was in the scrap iron business; it was in the salvage business; it was in the machinery business; that is, machinery, both new and used; it was in the belting business; it was in the machine shop business; it was in the glass scrap business; in the electric motor business and supplies,——

Q. You can leave out the rest of the merchandising businesses. Was it engaged in any other business?

A. Incidental to its normal business?

Q. Yes. A. Yes.

Q. What was that?

A. Helping to finance and lending money to other people [350] to help itself primarily, through goodwill, or to have a source of scrap iron and salvage material.

Q. Anything else?

A. Of course, it went into businesses that you might say were offshoots of its main business, such as going into the installation business such as plumbing. They were selling plumbing, and decided

(Testimony of M. R. Schnitzer.)

to go into installation. And then they decided to extend the Central Supply. They were using oxygen, and decided that since they themselves were large users, they could build a plant to manufacture it.

Q. Was the organization of this corporation a part of its regular business?

A. Yes. It decided to extend in 1928, for instance, and opened up the National Machinery Company.

Q. I think that is sufficient. Was any payment received on the second debentures until the second mortgage was satisfied?

A. No, sir.

Q. I notice the accounts that you have testified to, that is, the regular accounts receivable, and there were charges there for merchandise and cash advances. In other words, they debited cash advances on a regular merchandise account. Was that the custom of the Alaska Junk Company?

A. Yes.

Q. Did you in the course of your business ever overhear [352] Mr. Wolf make any remark about the investment that the Alaska Junk would make in Oregon Steel?

A. Yes.

Q. What was it?

A. Under the original plan he told me that the commitments of the Alaska Junk Company were \$62,500, and that although he was not too happy about it, he said that was good enough for his partner, Sam Schnitzer, was good enough for him-

(Testimony of M. R. Schnitzer.)

self and his wife. I believe it was in 1942 when Morris Schnitzer's difficulties began, and he could not take his subscription of \$125,000 and Mr. Wolf generally talked about it in the office, and he had discussions with me as to whether or not the Alaska Junk could stand it, and he said that he would go, on behalf of the Alaska Junk Company, to \$125,000, but that was all; and, as a matter of fact, he thought at that time,—this was at the time the RFC made the loan to the mill, that the Alaska Junk was through putting in any money because the debentures and the stock offset on the account were so great that anything that went to the mill in the future would have to be repaid immediately by the RFC. [352]

\* \* \*

Q. Now, I think in response to counsel's question, you testified that Alaska Junk made loans to organizations which purchased materials from it and which furnished an outlet for [371] its scrap iron?

A. I think you have it in reverse. The loans were generally made to companies, were companies who did purchase from it, that is true, but who mainly sold scrap to the Alaska Junk Company as waste or scrap material from manufacturing plant or machine shops for example.

Q. In other words, was it your testimony that they made loans largely to these firms, because they supplied them with scrap?



(Testimony of M. R. Schnitzer.)

A. Both ways. For example, Hesse-Ersted Iron Works received a loan in the form of a mortgage, and they became good customers; they bought our merchandise. In other words Steel Tank and Pipe Company sold us scrap iron, scrap from what they used in manufacturing.

Q. What was the first one?

A. Hesse-Ersted Iron Works, on which a mortgage was taken for \$65,000. I think that has been testified to.

Q. Was that a company that Alaska sold scrap to?

A. We didn't sell it to that company; we sold it to the stockholders of that company, Hall and Mears.

Q. Is there any company here, Mr. Schnitzer, that you mentioned, to which money was advanced, to which you also sold scrap iron?

A. We would buy scrap iron and sell it to the mills.

Q. If the answer is "no," I wish you would give it to me [372] as "no." I want you to concentrate and think of any other company in the same category with the Hesse Ersted Iron Works, where advances were made as in that case where the company as in that case, to which the advances were made, purchased scrap iron. Of course, I mean other than the mills, such as Bethlehem, which bought scrap.

A. Hesse Ersted bought machinery and supplies



(Testimony of M. R. Schnitzer.)

of that nature; the other firms I mentioned produced scrap iron.

Q. Did Hesse Ersted purchase machinery for their own use or for sale?

A. For their own use. I might, if you wish, state that there were many instances such as these deals, in 1934, 1935, 1936, such as the Western Foundry; there we supplied cast iron without receiving payment, taking it out in trade over a period of years; we advanced scrap iron and collected for it in trade over a period of time.

Q. You would receive merchandise from them to pay it off?

A. Yes. That was also true of the Vaughan Motor Works, about which my cousin testified this morning.

Q. I think you explained that in the Hesse Ersted case—actually it was Hall and Mears that made the purchases from the Alaska Junk, and not the corporation?

A. No. You asked me if I didn't sell the steel mill, or if we didn't sell the steel mill to Hesse Ersted; we sold [373] just the mill to Hall and Mears.

Q. I am not talking about the steel mill now.

A. The mortgage was made to the Hesse Ersted Iron Works, a corporation, of which Hall and Mears were principal stockholders.

Q. And what was the mortgage?

A. A \$65,000 loan which we gave Hesse Ersted,

(Testimony of M. R. Schnitzer.)

and bailed them out when they were in receivership.

Q. Just answer each question as we go along, and I will be able to understand it. Did Hesse Ersted buy any of the products that Alaska Junk had for sale?

A. Yes.

Q. What products?

A. Pipe; I believe some cast iron as distinguished from scrap iron; rails; electrical supplies, and virtually anything that they might need in the conduct of their business that we carried.

Q. Was that some stuff for resale?

A. They were not in the habit of re-selling; they were a foundry or machine shop.

Q. And these were materials that they needed for their operation?

A. Either for their operation or for re-manufacture.

Q. And in what proportions were their needs compared with what they needed for re-manufacture? Just what proportion [374] was it that they needed for their operation, just what did they need for re-manufacture, of that which they purchased from you?

A. I couldn't answer that question. When I say "re-manufacture," that might mean a myriad of things. In other words, they would do the melting, and, in addition to that, they might need pipe or an oiler or some component part of hoist.

Q. So they bought rail and steel which they themselves melted down?

(Testimony of M. R. Schnitzer.)

A. Either melted down or fabricated.

Q. Comparing the items in that category with the items that they purchased for their own use, equipment and that sort of thing, can you give me any estimate as to what that corporation was?

A. I have no way of guessing.

Q. There would come a time when they would have all the equipment that they needed?

A. Oh, in a large shop *there things* wearing out that have to be replaced, like belting, and so forth.

Q. Could you give me an estimate as to the difference between the two kinds of items that are mentioned?

A. I couldn't even guess.

Q. Do the books here show it? Are the books here from which you can make examination?

A. I don't think they are here. [375]

Mr. Marcussen: Are they here, counsel?

Mr. Jones: No; they are not.

Q. (By Mr. Marcussen): Now, the National Machinery Company was a corporation?

A. Yes.

Q. And what was its business?

A. New and used machinery and supplies; and I believe they also have the agency for the Fordson tractor.

Q. And how did it differ from the business of Alaska Junk, generally?

A. The only difference I could think of was that

(Testimony of M. R. Schnitzer.)

they did not handle scrap iron; they were not in the scrap iron or salvage business.

Q. And the Alaska did not handle the Fordson?

A. That's right.

Q. Is that the only difference?

A. The only major ones; and the Alaska Junk had agencies that the other did not have.

Q. Did anybody else own any stock in it?

A. There was only one other stockholder than the Alaska, and he was Mr. Nehl; he was the manager of the National Machinery, and he had been a former employee of the Alaska Junk. He had subscribed to some part of the stock, or to some shares; the number I could not tell you; and he was to pay for [376] them out of his share of the earnings, and when I came into the picture going over the books we found he never did pay for any of it in any of the subsequent years, and finally there was a compromise payment of \$500 for his subscription.

Q. Did Alaska Junk organize this corporation, or were they in it from the beginning, or was it an existing corporation?

A. They started in from scratch.

Q. I think you testified that they sold merchandise. An account of this company on Alaska books is identified in this record as Petitioner's 41, and that consists of the merchandise that was sold and also cash advances; is that right?

A. That's right.

Q. What is the nature of the merchandise sold?



(Testimony of M. R. Schnitzer.)

A. Could I see the books (indicating) ?

Q. What I am getting at, was it for resale ?

A. Yes; they were in the business of selling; so everything that we did sell them would be sold again.

Q. So Alaska Junk was really wholesaling to them ?      A. That is right.

Q. What is the proportion between the cash advances and the merchandise sold on that account ?

A. There are 49 double pages here. Do you want me to run through it and figure it out ?

Q. I think that would take too much time. [377]

Mr. Jones: There is a witness coming on the stand who has footed it up; he has footed up all the cash advances on this account and he will testify as to those.

Mr. Marcussen: Very well.

Q. (By Mr. Marcussen): Did you testify that the stock was paid for in that case by an offset against the account of National Machinery ?

A. I don't believe I mentioned that, because I don't know without looking at the accounts. I cannot tell from these records, because these records started in January 1928, and I believe the corporation was formed sometime in 1927; some of the sheets are missing, because they did not have the "Elliot Fisher System" at that time.

Q. Then I think the next item that you testified to is Petitioner's 42 for identification, pertaining to Central Supply Company ?      A. Yes.



(Testimony of M. R. Schnitzer.)

Q. Was that a corporation? A. Yes.

Q. In that case I think you testified that they subscribed to \$50,000 stock, and that payment of the stock was effectuated by an offset against this account?

A. That is correct, with the exception that the corporation was organized for \$5,000, and was paid for through offsetting entries, and the stock was subsequently raised to [378] \$50,000.

Q. And the additional \$45,000 was handled the same way? A. At that time?

Q. At the time they purchased the stock?

A. The assets of the company were what they advanced——

Q. What were the assets of the Central Supply; at the time \$50,000 was paid for by Alaska?

A. What were the assets?

Q. How much of the total assets were there in Central Supply? A. \$50,000.

Q. The assets were no more than the stock subscribed for?

A. I know the Alaska had about \$70,000 or \$80,000 put out; and they had either the equivalent such as accounts receivable, or something to offset it.

Q. Can you picture the balance sheet of the Central Supply, and give us a picture of the assets side of the balance sheet? A. I can not.

Q. All right. What were the assets at the time they had \$50,000 in stock as one of the items on the liability side?

(Testimony of M. R. Schnitzer.)

A. The Central Supply started out with Alaska Junk advancing it, whether it was \$5,000 or \$50,000. So the assets [379] were the equivalent of its liabilities.

Q. Were there any other assets besides the stock item of \$50,000?

A. Only the current accounts for merchandise sold currently and bought.

Q. And how would they compare with the \$50,000?

A. Very nominal.

Q. You stated that the accounts were handled with respect to the corporation in substantially the same manner as the accounts were handled in the case of Oregon Steel?

A. That is correct.

Q. Can you elaborate your answer on that?

A. Everything given to either of those corporations, whether it be in cash or merchandise, was charged; when the stock was issued, and whatever was carried forward; the only real difference was that Central Supply was successful and they paid off, and the Oregon Steel was not successful and we took a loss.

Q. Was there any difference—I will change that. Wasn't the entire difference between Central Supply and Oregon this, that in Central Supply the partners received for practically their entire investment in the organization, stock?

A. No.

Q. Isn't that true?

A. No; I think you will find that they had as

(Testimony of M. R. Schnitzer.)

much as [380] \$100,000 in there, and they received \$50,000 in stock.

Q. I think you said the balance sheet of the Central Supply, on the assets side, would show very little more than the \$50,000 of stock that was represented on the liability side?

A. I didn't say that. I said the assets side would be equivalent to the liability side, which, in turn, would be actually what the Alaska Junk had advanced, whether it was \$5,000, \$50,000 or \$100,000.

Q. But there were very nominal liabilities in addition to the \$50,000?

A. Other than the Alaska Junk?

Q. At the time the Alaska Junk had the \$50,000 of stock, what were the total other liabilities of the company?

A. I couldn't answer the question without looking at the books?

Q. Do you have the books available?

Mr. Jones: Central Supply?

Mr. Marcussen: Yes.

Mr. Jones: No.

The Witness: I will say that any liability that it had, other than the Alaska Junk was in current condition.

Q. (By Mr. Marcussen): Do you happen to know what was the greatest amount or the highest amount? We can check that on this exhibit—[381]

A. That's right.

(Testimony of M. R. Schnitzer.)

Q. What was the highest amount that the account ever reached? Just roughly.

(Hands document to witness.)

A. I can check that up. In addition to the \$50,000 capital, there was a high of \$60,329, making a total of \$110,000 plus.

Q. As of what date was that?

A. That would be August of 1942.

Q. And the next item that you testified was with respect to the Carleton and Coast venture. Will you state how their business compared with the Alaska Junk.

A. It was a single venture and was a combination of Alaska Junk and the Dulien Steel products; and the liquidation of this one major purchase, which primarily was a railroad and logging camp, purchased from the Reconstruction Finance Corporation, plus a small amount, or a smaller amount in the same area where other merchandise was located——

Q. Was there a Carlton there?

A. There was a town of Carlton. And the town itself—the railroad itself was known as Carlton and Coast.

Q. How about the other 50 per cent in the venture? Did the other party have 50 per cent in the venture? A. Yes.

Q. And who was that, again?

A. Dulien Steel Products of Seattle. [382]

Q. Dulien Steel Products?



(Testimony of M. R. Schnitzer.)

A. That is correct.

Q. How was it that you came into the picture?

A. The same as Dulien came into the picture.

Q. Did Dulien have it first?

A. There were two parts to that. There was a Trask Willamette Railroad, plus the Flora Logging Company part, plus the Yamhill Log and Lumber part which, I believe, the Alaska Junk bought and Dulien at this time purchased the Southern Pacific Railroad Company's rails in there. This was way off in the wilderness, a part belonging to one company and a part to another, and each one bought one section; one outbid the other in one of them. So, after it was over with we got together to make it one venture.

Q. In other words, the Alaska Junk and Dulien found themselves bedfellows in the dismantling of this Carlton and Coast venture?

A. In that each had merchandise in the woods, and there was a question of getting it out some way.

Q. Did Alaska bid on the whole thing?

A. Yes.

Q. In the part that Dulien got? A. Yes.

Q. Did Dulien do the same?

A. Yes. [383]

Q. So the Alaska Junk was successful in one part and Dulien was successful in the other; is that the way it was? A. That's right.

Q. And finding themselves in that situation, they got together to do the dismantling job so as to en-



(Testimony of M. R. Schnitzer.)

able them to enjoy all the economies they could get from such a procedure?      A. That is right.

Q. And when Alaska Junk bid on that job, were they following a procedure which was frequently done in their business? Was that their regular business, bidding on such projects as that?

A. Yes.

Q. I didn't quite understand your testimony on direct as to how they were repaid for the so-called advances, as you put it, on the Carlton and Coast venture.

A. That I believe was handled a little differently than many of them. Dulien and Alaska Junk each put in originally \$67,251.18, according to the ledger here, and subsequently Alaska Junk furnished materials and cash for working capital, because they operated independently of Alaska Junk, and as they operated and liquidated their merchandise they repaid Alaska Junk for the current advances and what not and ultimately paid off the major part of the original investment.

Q. Did that operation result in a loss to Alaska Junk?      A. Yes. [384]

Q. And did it result in a loss to Dulien?

A. Yes, equally.

Q. And how did Alaska Junk take that loss on its books?

A. That loss was taken after my time, and unless it is shown on the books, I cannot answer.

Q. When was the job completed?

A. I don't know whether it is completed now.

(Testimony of M. R. Schnitzer.)

Q. Do you recall what the years were that that took place?

A. It apparently started September 1, 1943. I left in 1944, and I see here book entries in 1945 and 1946 (indicating).

Q. Does it indicate to you that there is a final accounting on that ledger?

A. There is an open balance. I believe I heard that there were some tag ends still to be wound up.

Q. And that open balance is in the amount of how much?

A. It appears to be \$3,737.

Q. The date is January 3, 1945 (indicating)?

A. 1946.

Q. And these are balances as reflected in Petitioner's 44 for identification?

A. That is for the advances and merchandise supplied.

Q. Will you check that page? [385]

A. This doesn't have anything to do with this (indicating). That would be accounts receivable control.

Q. Then this accounts receivable was all paid off?

A. It appears to be.

Q. There was no loss on that?

A. Not on that account.

Q. Then how would the loss be handled, if there was a loss?

A. I am not with the company, I could not tell you.

(Testimony of M. R. Schnitzer.)

Q. When did you leave the company?

A. 1944.

Q. We are talking about their practices as in 1942 and 1943; and this is offered as an indication of their practice.

A. If I was still there I would make an entry and charge the balance to bad debts.

Q. Why bad debts?

A. Because the Carlton Coast owes Alaska Junk. I will take it back. In this case the accounts receivable is paid off. I would call it a business loss.

Q. An ordinary business loss in the case of Alaska Junk operating in a joint venture?

A. This one (indicating); the way it is handled, yes.

Q. I hand you Petitioner's 45 for identification, which pertains to the Marshfield Bargain House. What business were they in? [386]

A. How is that?

Q. What business was the Marshfield Bargain House in?

A. They were in the mill and yard machinery and supply business, and also the scrap business.

Q. Substantially the same business as Alaska Junk?

A. Yes, but on a much smaller scale.

Q. And where was their place of business?

A. In Marshfield.

Q. Did they supply scrap to Alaska?

(Testimony of M. R. Schnitzer.)

A. Yes.

Q. I think you stated that the accounts represent largely sales to the Marshfield Bargain House.

A. Both sales and cash; what you see here is an entry covering a period of approximately a year, all of which was reimbursed at one time by a credit for scrap iron, that is, we advanced the cash and merchandise which was paid for in scrap.

Q. And they returned scrap to you?

A. Yes.

Q. That was a procedure commonly *used Alaska* Junk in order to obtain scrap from its source of supply; is that correct? A. Yes.

Q. Do you know whether Marshfield Bargain House is a corporation? [387]

A. I have no way of knowing. I know the owners some, and I have always heard them referred to as partners.

Q. I guess we went a little backward in this procedure. Counsel presented you with the accounts for various small junk dealers and collectors, which was Petitioner's 49 for identification (hands document to witness). Those advances, again, represented advances to your source of supply for the purpose of procuring scrap iron?

A. To the smaller sources of supply.

Q. Who would be the small sources of supply?

A. Junk dealers; junk peddlers. Their names are here if you want to see them; some of them.

Q. How would these loans be effectuated?

(Testimony of M. R. Schnitzer.)

Would a junk dealer come in and say that he knew of a bit of junk that he could get, and that if he could get the money from Alaska Junk then Alaska Junk would get the scrap, that is, he would buy it and sell it back to Alaska Junk if Alaska Junk would advance the money? Is that the way it was handled?       A. Yes.

Q. And the next one here was M. Turn, which is shown on Petitioner's 48 for identification.

A. That's right.

Q. What was his business?

A. What was his business?

Q. Yes. [388]

A. His business was a conglomeration of new and used supplies, small machinery and furniture and scrap iron.

Q. With the exception of the furniture, his business as far as it went was similar to Alaska?

A. On a much smaller scale, confining himself to smaller supplies and equipment.

Q. But in kind, it was the same?       A. Yes.

Q. What merchandise did he buy from Alaska?

A. Splitting sledges, axes, pipe, pulleys, pipe-fittings, roofing.

Q. Would it be correct to characterize the relationship between Alaska and M. Turn as that of a wholesaler and retailer, respectively?

A. Jobber and wholesaler, or wholesaler and retailer.



(Testimony of M. R. Schnitzer.)

Q. Alaska Junk being the wholesaler and they the retailer?      A. That is right.

Q. Then when you said that a part of the advances in the account were advances of merchandise, what were you talking about?

A. No; I was talking about the other one; in this one it was cash advances; in the other one it was cash and merchandise.

Q. Didn't you testify with respect to M. Turn that it [389] was cash advances and merchandise?

A. Accounts of merchandise sold, and cash advances on scrap iron. He made a practice of paying his bills.

Q. A very happy practice in this business?

A. And very unusual.

Q. Was he a supplier of scrap for Alaska?

A. Yes.

Q. And were the advances that were made to M. Turn similar to the advances that were made to other suppliers, simply to pick up a certain batch of scrap and bring it in to you people?

A. That is right.

Q. By you people, I mean Alaska, of course?

A. That's right.

Q. I hand you Petitioner's 44, which relates to the Industrial Air Products Company.

A. That is right.

Q. That was a corporation, as I understand it?

A. That's correct.

(Testimony of M. R. Schnitzer.)

Q. Was that a corporation that was organized by Alaska?

A. By the owners of Alaska Junk and Morris Schnitzer; I believe there were one or two nominal stockholders in addition.

Q. How much stock did the partners of Alaska Junk and Morris Schnitzer buy in that organization? [390]

A. Alaska Junk bought \$70,000 worth. I don't know how much Morris Schnitzer bought, but it is my offhand impression that it was about half of that.

Q. And I think you testified that the stock was paid for by an offset against the account?

A. That is right.

Q. And what is the highest amount that that account ever got before the stock offset?

A. Before the stock offset?

Q. Yes?      A. \$76,000.

Q. And then immediately after the stock offset, what was the balance after the offset?

A. \$475.

Q. And what were the dates when the stock offsets were made?

A. November 1, 1941.

Q. And what was the highest amount that the accounts got to after the stock offset?

A. Approximately \$36,000.

Q. When was that?

A. December of 1942.

(Testimony of M. R. Schnitzer.)

Q. Have you ever had occasion to analyze or see the balance sheet of that company during any of these times that you have testified that these advances were made, which, I [391] understand, was from 1940 to 1943.

A. I remember seeing one or two statements, but I don't remember the figures.

Q. Do you have any recollection at all of what the total assets were?      A. No, sir.

Q. What other accounts receivable did the company have?      A. Which company?

Q. Industrial Air to outsiders?

A. I cannot answer that, because I had nothing to do with their books.

Q. I recall you saying in the case of Central Supply, those outside accounts were rather nominal?      A. That is right.

Q. You cannot say what they would be approximately of the Industrial Air Products?

A. I have no recollection of them.

Q. Mr. Schnitzer, I hand you Petitioner's 50 for identification, which pertains Munce and Pedrante, and I believe you testified that that account represents cash advances, merchandise sold, and supplies sold, is that correct?      A. That's correct.

Q. What was the business of Munce and Pedrante?

A. They were truck haulers and contractors; their business was largely dismantling of machinery and hauling [392] machinery and scrap iron and the like.

(Testimony of M. R. Schnitzer.)

Q. Did I understand you correctly on your direct testimony to state that the amount was paid off by the delivery of a truck by Munce and Pedrante?

A. Partially paid off.

Q. To the extent of about \$5,000, and then partially by performance of services; is that correct?

A. That's right.

Q. For Alaska by them; is that correct?

A. Not quite. The practice was, so far as repayment was concerned, to collect for a particular delivery; then they would give us a part of the cash that we gave them to apply on the account. And there were a number of payments of \$25, \$50 and \$100; a number of them; and towards the end they still owed us a balance of \$5,042.75, and they turned over to us a truck, which we, in turn turned over to the Industrial Air Products and charged Industrial Air Products and crediting them with the amount, and a \$42 balance was later settled.

Q. Was that one paid for by work done, or didn't you use some such similar expression?

A. I don't believe I used that expression in connection with this account. They would haul in, say, 15 tons and we would pay them a certain amount, which would include the dismantling, and so forth; we would pay them, say, \$100 for that and they would pay us back a part. [393]

Q. Do you mean that you had engaged them to do some work, for which you paid them \$100?

A. Yes; after it was done.



(Testimony of M. R. Schnitzer.)

Q. And instead of paying them the full \$100, you gave them \$50 or \$75?

A. No; I would give them \$100, and so much of it I got back; sometimes it was \$50 and sometimes it was \$25.

Q. And these cash advances, were they made for the purpose of securing credit?

A. The cash advances given to these people was for their use, and in paying for their men and equipment that way.

Q. Were they doing considerable work for your company?

A. Yes; they were doing quite a bit of work; trucking and hauling.

Q. What trucking was it?

A. Well, we would send them out to pick up a railroad; dismantle a railroad and load it on the truck and haul it into Portland. That is one instance that I can recall. Another instance was going up to a ship in Marshfield, loading the machinery on trucks and hauling it in to us.

Q. So the cash advances were for the purpose of enabling them to haul the scrap into Alaska?

A. Yes.

Q. And for the purpose, mainly, of enabling you to secure more scrap? [394]

A. Our scrap; again, they were doing the dismantling and delivering to us.

Q. I hand you Petitioner's 51 for identification, which pertains to Emil Nyberg. And I think you



(Testimony of M. R. Schnitzer.)

stated that this transaction covered a period within a year, 1937 from June to December?

A. That is correct; actually, June to November.

Q. What business was Mr. Nyberg in?

A. He was a contractor; originally a logger and contractor, so far as we were concerned. We had purchased a logging camp in the vicinity of Stevenson, Washington, and there was also a part of a railroad. The railroad in itself was very difficult to get at and easier for someone who lived in that vicinity to get at, because the weather was adverse and the terrain was stiff; so that you could only get in there at certain times. It was very steep and tough to work at. Nyberg lived in the vicinity and contracted to pick up the equipment in the woods, that is, the rails and the donkey engines in the woods, and to load them on a railroad spur at the spur up there, and then they were to be shipped from that point to the Alaska Junk in Portland as salvage. And, as I recall it, after preparing the scrap iron according to specifications, it was to be shipped to the steel mills.

Q. Do you know what railroad that was? That logging camp railroad? [395]

A. Yes, there were two of them; the Trask-Willamette Company or a subsidiary. I think it was the Trask-Willamette, and the Ryan-Allen Lumber Company.

Q. And Alaska Junk was the successful bidder on the dismantling of the railroad?

(Testimony of M. R. Schnitzer.)

A. As I recall it, this was direct negotiations.

Q. I think you testified that cash advances were made, in part?

A. Practically 100 per cent in this case.

Q. And then you testified there was some merchandise? A. \$30 worth.

Q. Out of a total?

A. Incidentally that \$30 was salvage that they took out of the camp; they wanted some windows and doors that were salvaged and we charged them \$30. The total amount was \$3,400, consisting of services performed—on the debit side, loans and advances which were made to them.

Q. It is not correct to say the advances were made for merchandise that you sold them?

A. That \$30.

Q. And cash advances were actually for the purpose of enabling him to undertake the operation for you?

A. The original advance was not given to Nyberg for supplies and equipment and labor, but we found at the end he had not paid his crew and we had to pay his crew, and we charged [396] his account back for the payment to the men for the payroll.

Q. So that the cash that was advanced was advanced to him for the purpose of enabling him to carry out his contract with you to secure the salvage in that operation? A. That is correct.

(Testimony of M. R. Schnitzer.)

Q. And I think that your counsel stated that in some instances, advances had been made before merchandise had been sold in connection with this operation, and I think you testified that that was correct.

A. I think you used the wrong word; before the merchandise was delivered. You said "sold."

Q. The only merchandise that was delivered?

A. These advances were given to these fellows so that they could deliver the scrap. When they delivered the scrap we paid them the contract price, and then we attempted to get back our advance. This refers to merchandise that was, a little of it, sold to Nyberg, which was something personal that he wanted.

Q. Outside of that sale there was no merchandise advanced?

A. Not on this account.

Q. To Mr. Nyberg?

A. That's right.

Q. And the cash advances were merely for the purpose of enabling him to carry on his contract with you?

A. That's right. [397]

Q. I hand you Petitioner's 52 for identification, which is the account of R. Pedrante. What was Mr. Pedrante's business?

(Hands document to witness.)

A. Originally a trucker, and later a trucker and contractor.

Q. What was it when these advances were made?

A. I believe a trucker; trucker and contractor.

Q. When you use the term "contractor," do you

(Testimony of M. R. Schnitzer.)

use it to mean a person engaged in the business of contracting with you to haul out the scrap on the job?

A. I would like to correct myself there.

Q. Surely.

A. Pedrante in this case was a trucker, and later a trucker and contractor. I distinguish between the two in this respect, in that Pedrante would go work or where our crew was wrecking; he would take his truck there and have it loaded and haul it then to the Alaska Junk in Portland, or wherever was designated. In other words, the actual dismantling work was being done by someone else than Pedrante. As a contractor and trucker I referred to him whereby he did the dismantling and the loading and hauling.

Q. In this case, which represents the time December 1938 to 1940, he merely acted as a trucker for Alaska Junk?

A. That's right.

Q. Where did he operate? What particular territory did [398] he cover?

A. Any place in the State of Oregon or Washington. As I recall in this particular instance, one was up around Enterprise, Oregon, and the other was from Mukilteo, Washington.

Q. These advances, were they made for the purpose of enabling him to carry out and finance his trucking contract with Alaska Junk?

A. Yes.

Q. So far as you know, as advances were made to him, were they ever made if he had no contracts for trucking with Alaska?

A. Definitely not.



(Testimony of M. R. Schnitzer.)

Q. Definitely not? A. That's right.

Q. Is it true generally that all the concerns that we are talking about were in the same category with respect to that?

A. If we couldn't make some money out of it or get some benefit out of it, we wouldn't be interested in making the loan.

Q. You would not be interested in making the loan? A. Not as a loan.

Q. Now, in this particular case, did Alaska Junk sustain a loss on that account? A. Yes. [399]

Q. How much of a loss? A. \$2,723.47.

Q. And do you know what the contract covering that period of time called for in terms of gross payments to him for his services of trucking?

A. Will you repeat that?

Mr. Marcussen: Will you read that, Mr. Nelson, please?

(Whereupon the last question was read aloud by the reporter as above recorded.)

A. I seem to remember a figure of six and one half dollars a ton from Enterprise.

Q. (By Mr. Marcussen): I am thinking in terms of the total amount?

A. No; I could not tell you.

Q. What was done on the books of Alaska with that loss? A. Charges to bad debts.

Q. It was not charged as a part of the cost of trucking? A. No, sir.



(Testimony of M. R. Schnitzer.)

Q. The effect, insofar as the business of Alaska is concerned, would be the same?

Mr. Jones: That calls for a conclusion on the part of the witness.

Mr. Marcussen: You have called for a lot of conclusions. [400]

The Witness: Still the net result.

Q. (By Mr. Marcussen): The net result is the same?

A. Still the net result is the same; you would like to know why there was a loss?

Q. Well, I should beware of a horse bearing gifts; but if you wish to state why there was a loss, go ahead.

A. He got mixed up in another hauling contract which was not very good for him. At that time he was heavily involved, outside of this obligation, to some finance company. One of his trucks was a total loss in an episode and fire, not covered by insurance, and the financing agent repossessed the truck, and he was left with nothing and no prospects, and that was the end of Mr. Pedrante, and we could not collect the money.

Q. I suppose, if that had not happened, there is not a reason to believe that accounts would not have been paid up? A. That is correct.

Q. I hand you Petitioner's 53 for identification, which is the account of the Medford Bargain House of Medford, Oregon, and I ask you to state what was the business of that company?

(Testimony of M. R. Schnitzer.)

A. Very similar to the Marshfield Bargain House and Alaska Junk on a small scale.

Q. And I think you testified that the advances which are charged on that account were cash advances on merchandise [401] sales?

A. That's right.

Q. And did Alaska stand in the relationship of wholesaler and retailer in that operation?

A. So far as merchandise was concerned.

Q. Alaska Junk was the wholesaler, again, and they were the retailer? A. That is correct.

Q. And were purchasing materials?

A. Yes.

Q. Were they also engaged in the business of contracting with Alaska Junk for the purchase scrap and salvage, or for the production scrap and salvage operations?

A. No; they would sell Alaska Junk scrap, and would borrow or get another advance, either merchandise or cash, and in this case, both; and then they would repay with scrap iron.

Q. Was their situation similar to some of the others that you have noted?

A. Similar to M. Turn and Marshfield Bargain House.

Q. And did they come to you and say, "We have a deal for some scrap. Are you interested? If you are we will get it."?

A. That's right.

(Testimony of M. R. Schnitzer.)

Q. And say, "We will protect you and deliver the scrap to you."? [402]

A. That's right.

Q. And those organizations got the profit and Alaska would get the scrap?

A. We figured to make a little profit; but we wound up with the scrap.

Q. And you would get the scrap and make a little profit on the scrap resale?

A. That's right.

Q. I think you testified with regard to the Medford Bargain House that some of the advances had been made while they were in debt to Alaska?

A. Yes.

Q. What do you mean by that?

A. They had a balance for merchandise and then they came in and said, "Give me one thousand," or "Give me two thousand, and we will deliver to you in three months, or six months, sufficient scrap to offset the entire amount."

Q. Just a mere happenstance, wasn't it?

A. Well——

Q. It was just a mere fortuitous circumstance that they happened to owe you money for goods Alaska had sold them, and you happened to have charges on the books for goods that you had sold them at the time?

A. With this difference; some of them could do like Max Turn did, for instance, he preferred to keep his bookkeeping [404] straight by paying for

(Testimony of M. R. Schnitzer.)

his merchandise, and later offsetting the cash advances for scrap delivered. These people wanted as much as they could to pay us off later in scrap.

Q. The only difference is that they ran with the account with respect to the goods you had sold them—they were slower pay, in other words? Is that right? A. Yes.

Q. I think you testified about Plumbing and Heating Sales Company? A. Yes.

Q. I hand you Petitioner's 55 for identification. That was a corporation, as I recall it?

A. Yes.

Q. And Alaska Junk purchased stock in that organization? A. Yes.

Q. Did Morris Schnitzer? A. No, sir.

Q. Did Alaska Junk organize this company?

A. The Alaska Junk and Mr. Shea.

Q. How much stock did Alaska Junk take in the company?

A. I believe \$3,000 which was offset to the account.

Q. \$3,000? A. \$3,000.

Q. Do you know how much stock Shea had in it?

A. He subscribed \$2,000, but never did pay for it. [404]

Q. Was the payment for the stock, as I understood you to testify, effectuated by an offset against the account? A. Yes.

Q. At the time of the offset, or just prior to the offset, what was the amount of the account?



(Testimony of M. R. Schnitzer.)

A. \$8,700 in round figures.

Q. What was the date?

A. The date of the entry was March 20, as of January 26, 1940, when the company started. It was three months later when they had actually advanced \$8,700.

Q. And then they offset \$3,000 against that?

A. That is right.

Q. And what is the highest amount that account reached after the stock was issued?

A. \$39,000 odd dollars.

Q. When was that? A. June of 1941.

Q. Who was the manager of that company?

A. E. A. Shea.

Q. The advances, as I recall were cash and merchandise? A. Yes.

Q. The merchandise was sold by Alaska, was it, to this company? A. Yes.

Q. In effect, was Alaska again the wholesaler and this [405] company the retailer?

A. Yes. In this case, the company, the Plumbing and Heating Sales Company, were more than retailers; they were installers as well as retailers; they were in the business of installing plumbing as well as selling plumbing.

Q. They were plumbing contractors?

A. Yes.

Q. And as plumbing contractors, I presume they sold materials on some occasions, and, as you testified, on other occasions they installed materials on contract? A. That's right.



(Testimony of M. R. Schnitzer.)

Q. Referring now to the testimony about the bank loans and the interest rate that Alaska was required to pay. Do you know whether Alaska ever received money for less than 6 per cent?

A. Not from the First National Bank until sometime after I had left there. I am not speaking about the 20's; in the early 30's it was 7 per cent, and during a large part of my stay there it was 6 per cent. Subsequent to my stay there I understand they did get it for considerably less.

Q. But prior to 1944, they never had any 4 per cent loans that you know of?

A. No, definitely not, except that there were some 3 per cent loans secured by cash value of life insurance.

Q. Do you know whether the partners of Alaska Junk ever [406] endorsed the notes of Oregon steel?

A. I beg your pardon.

Q. Do you know whether the partners of Alaska Junk ever endorsed the notes of Oregon Steel?

A. Which notes?

Q. The First National Bank?

A. I don't know.

Q. Referring to your testimony concerning your advice to the partners of Alaska Junk concerning how much they could afford to put into this Oregon Steel venture, I think you stated it was your advice that they could not exceed \$125,000, which they eventually agreed to take in stock?

A. That is right.

(Testimony of M. R. Schnitzer.)

Q. Now, isn't it just as easy to lose money on these advances that were made?

A. These losses?

Q. Isn't it just as easy to lose money this way on these advances as it is on the stock?

A. There were losses.

Q. In other words, it doesn't make any difference, Mr. Schnitzer——

Mr. Jones: If the Court please, I will object to that as argumentative.

Mr. Marcussen: If your Honor please, there is no argument with the witness; there is nothing argumentative [407] about it.

The Court: I think this should be permissible on cross-examination. He testified that he said that they could not afford to buy any more stock. I will overrule the objection.

Mr. Jones: May I have an exception?

The Court: It is noted.

Q. (By Mr. Marcussen): How do you account for it, Mr. Schnitzer, that actually they had advanced several hundred thousand dollars in that account, hadn't they? A. At what point?

Q. Over a period of years to Oregon Steel?

A. Yes, they did.

Q. And can you recall the date on which they increased their holdings of one third to two thirds?

A. I think you have it there (indicating document); approximately December of 1942.

Q. Would you check on Exhibit 26, which is the

(Testimony of M. R. Schnitzer.)

general account of Oregon Steel on the books of Alaska, and ascertain what was the balance in that account on the date in question in December of 1942?      A. \$299,000.

Q. I think you testified that that was the amount of the balance as of October 31, 1942? [408]

A. That happened to be right.

Q. And that on November 30, I think you stated that on November 30 the balance was \$331,000?

A. \$301,000.

Q. Oh, I see. What was the highest balance in the month of December there, without splitting hairs: just generally?      A. \$572,000.

Q. As of what date?      A. December 31.

Q. Is that the date on which they had this understanding?      A. No, sir.

Q. What was the date?

A. I believe it was during the month of November; or the latter part of October.

Q. I think you testified it was December sometime?      A. What was that question?

Q. When was it that you undertook to reverse the ratio of the stockholdings?

A. Sometime in December.

Q. Sometime in December?

A. That's right.

Q. That \$500,000 figure that you mentioned, was that in December 1942?

A. Yes, that was after the \$100,000 advance to working capital, and also a payment to the First

(Testimony of M. R. Schnitzer.)

National of a [409] \$100,000 note, and it was after the RFC loan, and after the stock was issued, or was supposed to have been issued,—let us put it that way.

Q. What was the amount in December?

A. \$301,000 at the beginning.

Mr. Marcussen: Counsel, may I ask when did you fix the date in December for the undertaking on the part of Alaska to take two thirds of the stock?

Mr. Jones: I don't know; it was sometime in the month. It was an oral arrangement, and that is as near as I can place it.

The Witness: May I suggest something?

Mr. Marcussen: Yes.

The Witness: If the agreement was in the early part of December, the fifth or sixth or thereabouts, the girl at that time would not have completed her posting for November, and the figures we have used, some figure of \$299,000, would not be the November figure.

Q. (By Mr. Marcussen): What are you referring to?

A. This \$299,000 figure. With reference to the entry later of the \$174,000 of debentures and \$125,000 of stock; with the \$174,000 of debentures and the \$125,000, that was intended to wipe out the account at that time.

Q. How do you reconcile the advice which you gave to [410] Mr. Wolf that they could not afford



(Testimony of M. R. Schnitzer.)

to take any more stock than \$125,000, with the fact that they already had at that time, that is, the Alaska Junk had a total investment of \$299,000 or \$300,000 already?

A. There are two answers to that, or, rather, two phases to that. In the first place, during this particular period they anticipated that the mill would be in operation during the middle of June of 1943, and that the mill would be making a profit and would be able to retire in a comparatively short time any obligations which they had, which, of course, would not include capital stock. On the other hand, capital stock is a frozen fund, and that capital stock of \$125,000 along with the capital stock in Industrial Air, along with the capital stock in Central Supply, combined with the open accounts which were not at that time liquid, and which were in very substantial sum, not too far from the total capitalization of the Alaska Junk,—with the addition of frozen funds,—if they were going to the Bank to borrow some money, the Bank would turn them down in view of the fact that their capital was in frozen assets.

Q. By “frozen,” you mean stock and advances to these companies that we have been talking about?

A. That is right.

Q. Weren't the so-called advances, as distinguished from the capital stock, just as frozen as the capital stock at the [411] time?

A. These accounts?



(Testimony of M. R. Schnitzer.)

Q. Yes.

A. The difference was that the mill was expected to start producing in six months, that is, six months later, and to pay off; but they could not possibly pay off that stock.

Q. If the mill had gone to producing and began making \$50,000 monthly profits, the stock would have been indeed good collateral for any loans which the company would have needed from the bank?

A. It seldom, however, has ever had to resort to collateral. The fact is, if the mill had profits, it had this obligation of \$174,000, *together the* \$125,000 investment,—in that case the Alaska Junk would not have to use collateral in order to get money.

Q. I don't know whether I understand you.

A. If the mill had made \$50,000 a month profit, it would have soon cleaned up its current obligations and there wouldn't have been any collateral needed.

Q. The money in any event was tied up, whether it was tied up in stock or tied up in advances?

A. That's right.

Q. Assuming it were true that the partners of Alaska Junk expected to get paid back on their open account out of profits, the fact was that the advances were made right from [412] the very beginning in order to establish and found this mill? Is that correct?

A. That's right.

Q. So it must have been considered by them,

(Testimony of M. R. Schnitzer.)

was it not, there would be considerable delay before they could expect repayment? Isn't that correct?

A. No; they figured they would start getting their money back in the middle of 1943.

Q. The middle of 1943, that still would be two years from when it was organized? What is the first entry in that account? Isn't it true it was October 1, 1941?

A. That is right; for \$10,000.

Q. I think that is sufficient, Mr. Schnitzer. Now, I think you stated that some of the funds that were advanced to Oregon Steel were used to pay suppliers. Suppliers of what?

A. Equipment for the construction of the mill and supplies in the operation of the mill.

Q. What supplies in the operation of the mill?

A. I never was in the mill to see what they actually bought, but in a normal operation of a mill such as that, you would include virtually everything from waste to coke, and everything that goes into the manufacture. I think the word "alloys" would be better, and what not.

Q. They could not have needed very much of that, because they operated only about six weeks or so? [213]

A. That part of the supplies was apparently a nominal figure.

Mr. Marcussen: May I ask counsel whether he proposes to establish in the evidence what proportion of the advances made in the general account,

(Testimony of M. R. Schnitzer.)

namely, Exhibit 26, were in form of the four categories that this witness has testified to?

Mr. Jones: We have them broken down into three: cash advances, merchandise sold, and the third-party vendors bills paid. That is not broken down as to whether Alaska or Oregon Steel placed the order, but we have it in those three categories.

Mr. Marcussen: May I have Exhibit 6, please?

(Clerk hands document to counsel.)

Q. (By Mr. Marcussen): I hand you Exhibit 6, and refer you to the \$83,000 on page J-23, which I think you testified represented the adjustment that was made between Morris Schnitzer and Alaska Junk to cover the guarantee agreement which they had?

A. Yes.

Q. Now, can you tell me how that amount was computed?

A. I can read my entry.

Q. I wonder if I were to give you a slip of paper, whether you would quickly take the figures and make an analysis of that amount?

A. I can do it better than that. I can ask Mr. Johnson [214] for the original computation; he has got it.

Mr. Marcussen: Will that be in evidence, counsel?

Mr. Jones: Yes.

Mr. Marcussen. I will withdraw the question from this witness, if your Honor please, and I am about to conclude my cross-examination of this wit-

(Testimony of M. R. Schnitzer.)

ness; however, I would like to have a five minute recess to look over my notes.

The Court: Yes, we will take a five minute recess.

(Whereupon a five minute recess was taken.)

Mr. Marcussen: No further cross-examination.

The Court: Do you have any further questions?

Mr. Jones: Yes, I have about 3 or 4, your Honor.

### Redirect Examination

By Mr. Jones:

Q. Mr. Schnitzer, where was the National Machinery Company located?

A. In Eugene, Oregon.

Q. Referring you to the National Machinery Company account, I believe it is Exhibit 41, is it not?

A. Yes, I believe so.

Q. I am handing you National Machinery Company account, and I want you to state whether there was a bad debt there?

A. Yes, we wrote off \$30,000 odd in 1933.

Q. I will refer to Exhibit 56 and ask you if, in part,—if this bad debt is reflected on the Exhibit?

A. Yes, sir.

The Court: What exhibit do you have reference to?

The Witness: This exhibit is the Treasury Department Report on the return for the year 1933.

The Court: What is the number?

Mr. Jones: It is 56.

(Testimony of M. R. Schnitzer.)

The Witness: 56.

Q. (By Mr. Jones): What was the tax return for 1933? A. What is that?

Q. I would like to show you the tax return for 1933; I believe it is Exhibit 29 (hands document to witness)? A. That's right.

Q. Can you state whether on Exhibit 29 the same bad debt is indicated for the year 1933?

Mr. Marcussen: If your Honor please, I think this inquiry is immaterial, and Respondent objects to it on that ground; also the characterization of an immaterial matter as a bad debt.

The Court: I think counsel brought out on cross-examination matters along the same lines. I will overrule the objection.

Q. (By Mr. Jones): Well now, do you know whether the National Machinery Company,—what is the amount of the National Machinery bad [416] debt as indicated on Exhibit 41?

A. \$30,437.17.

Q. And what was the amount of the bad debt deduction taken on the 1943 tax return?

A. \$38,900.18.

Q. And was that allowed as shown by the revenue agent's report, Exhibit 56?

A. Yes. There is a note to the effect that it appeared that a bad debt of \$38,900.18,—that every effort had been made to collect it and it was charged off.



(Testimony of M. R. Schnitzer.)

Q. Do you know whether that item of \$30,000 is in the \$38,000 item? A. Yes.

Q. Was that debt incurred through advances of merchandise?

A. Advances made in merchandise, services, or cash.

Q. Will you give us an example of an advance of merchandise?

A. An example of an advance in merchandise?

Q. Yes.

A. Merchandise given without immediate prospect, or merchandise sold beyond regular treatment.

Q. It is not the same as selling merchandise on credit?

A. It is, but only on different terms. I think you are referring to sales such as merchandise given to the Medford [417] Bargain House. Normally bills will be due the 10th of the month following the date of sale. But when we referred to merchandise advances, it might mean that they would be paid out of merchandise, which might mean three months or six months or a year.

Q. I see. My attention has been called to the fact that in mentioning the accounts, Exhibit 43 was not called to your attention. I will just briefly hand it to you here and ask you to state what Petitioner's 43 for identification is?

A. These are the original ledger sheets of the Alaska Junk Company from its accounts receivable ledger, covering the account of Schnitzer Steel

(Testimony of M. R. Schnitzer.)

Products Company from July of 1936 until March 31, 1948.

Q. Will you state what the items on there are?

A. What do you mean?

Q. Will you give the general categories of the items there?

A. This is a combination of merchandise and cash advances to Schnitzer Steel Products.

Q. There are cash advances on there?

A. Yes.

Q. And who was Schnitzer Steel Products?

A. Morris Schnitzer.

Q. Did the partners of Alaska Junk have any interest in Schnitzer Steel Products? [418]

A. No, sir.

Q. How were those advances, cash or merchandise or funds, to the Schnitzer Steel Products made by Alaska?

A. In the same way as to any other firm.

Q. How were they repaid?

A. They were paid partially in scrap iron and in other merchandise which they would salvage from their operations of their own; and in cash.

Mr. Jones: You may cross-examine.

### Recross-Examination

By Mr. Marcussen:

Q. With respect to Schnitzer Steel Products, referring to Petitioner's 43 for identification, Mr. Schnitzer, these cash advances that were made, were

(Testimony of M. R. Schnitzer.)

they also made to enable Schnitzer Steel Products Company to secure scrap for Alaska Junk?

A. In some cases.

Mr. Marcussen: Will it be brought out eventually what the porportion was for cash?

Mr. Jones: Yes.

Q. (By Mr. Marcussen): And in other instances?

A. To help the son of one of the owners to get along.

Q. To help the son of one of the owners to get along?

A. To help the son of one of the owners of Alaska Junk [419] to get along in his business.

Q. Morris Schnitzer is the son of Sam Schnitzer, one of the owners of Alaska Junk?

A. That's right.

The Court: I would like to ask the witness a question. What relation are you to any of the parties?

The Witness: I am a nephew, sir.

The Court: You are a cousin of Morris?

The Witness: That is right.

Mr. Jones: What relationship are you to Manuel and Morris Schnitzer?

The Witness: They are brothers.

Q. (By Mr. Marcussen): Calling your attention to Petitioner's 41, which is the account of National Machinery Company. I think you testified in connection with that account as to what was meant by merchandise advances.

(Testimony of M. R. Schnitzer.)

Mr. Jones: Not in connection with that account, but just generally.

Mr. Marcussen: All right. Just generally.

Q. (By Mr. Marcussen): As to all the accounts that we *having* been talking about this evening, is it your testimony that they were all longer pay accounts than the usual accounts?

A. If I understand your question correctly, I understand [420] you to mean, are they all slow pay,—is that right?

Q. I am sorry, I didn't hear you. Will you read the answer, please.

(Whereupon the answer of the witness was read aloud by the reporter as above recorded.)

Q. (By Mr. Marcussen): Yes.

A. No; may I add something?

Q. Surely.

A. You asked me if some of these,—how we treated the balances. I told you that they were handled as bad debts. I want to add, in the case of National Machinery and in the case of Plumbing and Heating Sales Company, we did that; but where we made some recoveries later, as we did in some of the accounts, we credited it back to recovery.

Q. You will recall on cross-examination that we had considerable discussion about a number of companies; I think I have them all listed on the list that I hand you here (hands document to witness). On your direct examination it was brought out that

(Testimony of M. R. Schnitzer.)

the accounts for those companies and individuals arose through cash advances, in some instances, and merchandise sales in other instances. Nevertheless, in each instance there was both merchandise and cash?      A. No.

Q. There was not? [421]

A. In some instances it was cash.

Q. In some cases where contractors were hauling likewise it was cash?      A. That is right.

Q. With the exception of those, the advances consisted of both cash and merchandise?

A. Here is another one; Steel Tank and Pipe was cash.

Q. Now, where merchandise was mentioned in respect to those accounts, they were merchandise sales in the course of the Alaska Junk Company's business, were they not?      A. That is right.

Q. And in some instances, it is your testimony that they were slower pay, from three to six months, instead of ten days?

A. In some instances, because of that arrangement, they were slow to pay.

Q. Because of the arrangements you made with them?

A. It would be all right not to pay until they got some scrap iron.

Q. Can you tell what the arrangements would be in some cases?

A. For example, in the case of Medford Bargain House, they bought merchandise which was added



(Testimony of M. R. Schnitzer.)

to the accounts, and combined with the cash we advanced, with the understanding that it would be paid with scrap which they delivered some [422] months later.

Q. In other words, you made sales to those companies, and it happened that they were companies that were engaged in picking up scrap on salvage operations? A. That's right.

Q. And those operations were frequently over an extended period of time, is that correct?

A. That is right.

Q. And that is what you meant by special arrangements in those cases? A. Yes.

Q. And the understanding would be, since they were also customers of Alaska, they could reimburse Alaska and pay for the merchandise that Alaska had sold to them, by delivering to Alaska scrap, as a part of the arrangement?

A. That is true, but coming back to the Medford Bargain House, where they purchased merchandise and did not pay for it in one year's time, or in other instances where it was not paid in 30 days, where it was a longer time, they had made arrangements for those terms.

Q. They had made arrangements for those terms? A. Yes.

Q. This \$30,000 loss in connection with the National Machinery Company, was that in respect to merchandise sold to that company? [423]

A. Largely.

(Testimony of M. R. Schnitzer.)

Mr. Marcussen: That is all I have.

Mr. Jones: **Just a minute.**

### Redirect Examination

By Mr. Jones:

Q. Will you look into the accounts in there and give some indication of what they show with respect to cash advances?      A. What accounts?

Q. National Machinery.

A. National Machinery?

Q. Yes; or the bills paid for National Machinery.

A. I want to point out again, Mr. Jones, that this is not complete; it starts in January 1928, and they had been operating for several months; and prior to that the books had been kept on a different basis, on different kind of paper than here.

Q. Tell me, is there ever any balancing off in there? Did they ever strike a balance?

A. No.

Q. That is an account that was completely unbalanced and unliquidated to the end?

A. That's right.

Q. Is there any evidence of how much cash there is in that?

A. I don't know whether you can get that information. [424]

Q. What do you consider with respect to bills paid; are they in a category of merchandise furnished or cash advances?      A. Cash advances.

Q. By that you mean bills paid by Alaska on

(Testimony of M. R. Schnitzer.)

behalf of this company here, the National Machinery?

A. Yes; you will find those in particular at the tail end of the account.

Mr. Jones: No further questions.

Mr. Marcussen: No further questions.

The Court: You may stand aside.

(Witness excused.) [425]

\* \* \*

## PROCEEDINGS

June 12, 1948—9:00 A.M.

The Court: You may proceed.

Mr. Jones: Mr. Monte Wolf.

Whereupon,

## MONTE L. WOLF

called as a witness by and on behalf of the Petitioner, having been first duly sworn, was examined and testified as follows:

### Direct Examination

By Mr. Jones:

Q. Will you state your full name?

A. Monte L. Wolf.

Q. Are you one of the Petitioners in this case?

A. Yes.

Q. You are the son of Harry J. Wolf and Jennie Wolf?      A. Yes.

Q. Harry J. Wolf, one of the Petitioners?

(Testimony of Monte L. Wolf.)

A. Yes.

Q. You are a brother of Blossom Goldstein and Charlotte Cohon? A. Yes.

Q. Who have already testified?

A. That is right. [435]

\* \* \*

Q. When did you start working for the Alaska Junk Company?

A. Ever since I was a little fellow. I used to go there after school when I was about nine or ten years old, and on Saturdays, and I used to go down there with the folks and go to work. In those days, the early days, I used to have a truck,—

Q. Now, since when have you devoted your full time there? A. Since 1921.

Q. Did you ever have any experience in steel mills? A. No, sir.

Q. Did your father? A. No, sir.

Q. Now, what were your duties at the Alaska Junk Company during the years 1941, 1942 and 1943?

A. My duties were confined to buying and selling, and [452] helping with the organization as far as the personnel was concerned of the Alaska Junk.

Q. Did you have anything to do with pricing?

A. Yes.

Q. Explain that?

A. Whenever a charge was made, even after it had been priced by the head of the particular department, it had to either go through my hands or

(Testimony of Monte L. Wolf.)

Manuel Schnitzer's hands for correction or checking. Every charge before it went to the bookkeeper to be posted, it had gone through from anywhere to three to five hands.

Q. At what price was the merchandise sold to Oregon Steel?

A. At the regular prevailing market prices. Piping is based upon Moore's Pricing Manual.

Q. What do you mean by the Moore pricing?

A. The Moore price is the price that all of the organized dealers in pipe and plumbing use as a basis.

Q. Does he get out a list of some kind?

A. Yes, they have a list of iron piping and plumbing; and in each division it states the retail price and the wholesale price, and so forth.

Q. What is that called?

A. That is called the Moore Price Book.

Q. Would machinery be priced in it? [453]

A. Machinery would be priced on a percentage of the list price. The general usage before the war was that if a machine was in reasonably good condition, and it could be put in operation, it would be priced at fifty per cent of what it cost new.

Q. Do you have or did you have a factory list of those things?      A. Yes.

Q. And were they used in this pricing?

A. Particularly the items that we concerned ourselves with, that went into the mill, such as supplies of pipe and steel,—we are steel jobbers, and



(Testimony of Monte L. Wolf.)

we have a regular list from the steel jobbers as to the price of steel.

Q. The prices that you charged, how would they compare with the charges to purchasers, other purchasers of the same class of merchandise?

A. Those prices were the same prices that we charged to any other industrial concern.

Q. Were you present at any time at which a conversation took place in which your father or Mr. Schnitzer engaged concerning the investment in Oregon Steel?      A. Yes.

Q. Will you tell us what those conversations were?

A. My father and mother had agreed with Mr. Schnitzer and the Schnitzer family that, as far as the Alaska Junk [454] Company was concerned, all that they wished and saw clear to invest in the steel mill was \$62,500; that was about 625 shares, or thereabouts. In the latter part of 1942, I remember there was a conference in the office where Morris Schnitzer and his father came in and started talking to my dad, stating that it would be necessary for the Alaska Junk to take more stock. My father said that he didn't want to put any more in stock, but he said he would have to find out; and he talked it over with mother. Morris Schnitzer said, "I have 1250 shares, and it is more than I can carry, and I would like to work it out so that I could turn half of that over to the Alaska Junk," which would mean that he would have one third, and the Alaska Junk

(Testimony of Monte L. Wolf.)

would have two thirds. So, they discussed that, and my mother and father agreed,—

Q. Do you know whether there was ever anything said with respect to any more than that to be put in?

A. No, because I know that my father was rather close with the personnel, and he was very close to our bookkeeper, and he knew the situation pretty well, and he talked over with the accountant, and he didn't want to invest any more because it would affect the freedom of the Alaska Junk to carry on other functions of the business if too much money was put into that one project.

Q. Do you know whether the Alaska Junk did any business with Oregon Steel? [455]

A. Yes, we did; we sold them scrap iron, and from the beginning they have kind of favored us when new steel was hard to get,—which is very difficult to get,—and they have sold us new steel because we are steel jobbers, and we do get a quite a lot of steel from them today.

Q. How long had that situation continued since the Alaska Junk sold Oregon Steel to Mr. Hall and Mr. Mears?

A. We have been doing it right along; that situation has continued right along.

Q. And ever since they started, they have been selling you steel?      A. That is right.

The Court: Does your family or any of them own any stock in the Oregon Steel?

(Testimony of Monte L. Wolf.)

The Witness: No; when it was sold out, it was sold out at one time; and it was sold out because the partners, the men and the women decided it was the best that they could do at the time.

The Court: Alaska Junk has no interest at all in Oregon Steel today?

The Witness: It has no interest in the steel mill whatsoever, outside of what goods they have.

The Court: Don't they have note interest?

The Witness: That is right; they have a note interest. [456]

The Court: Those are the mortgage notes?

The Witness: Mortgage notes; yes.

Q. (By Mr. Jones): Do you know of your own information whether there was any intention on the part of Alaska Junk Company to invest more than their final investment in the Oregon Steel? I mean, in the capital stock?

A. No; it was never intended to put any more in.

Q. My question is, do you know that of your information? A. Yes, I know.

Mr. Jones: All right. You may cross-examine.

### Cross-Examination

By Mr. Marcussen:

Q. Is there a great demand for scrap steel now?

A. Yes.

Q. Scrap iron and steel? A. Yes.

Q. I presume that is reflected in the prices? Are you aware of that?

(Testimony of Monte L. Wolf.)

A. Yes; the prices today for prepared scrap are \$26 per gross ton; that is what we receive from the steel mills.

Q. Since November 23, 1943, do you know whether Oregon Steel has purchased considerable amounts of scrap from Alaska Junk and Morris Schnitzer?

A. Yes, and not only from them; they have purchased from [457] others too.

Q. Can you tell me whether they have wanted to purchase more than they actually had purchased; did you always have enough?

A. No; Alaska Junk has never had enough to take care of their needs.

Q. In the servicing of your customers of Alaska Junk, do you attempt to make a fair and equitable distribution to your customers?

A. Yes, because of the fact that we are steel jobbers, if we did not give the steel mills the scrap, naturally they would have no incentive to give us new steel.

Q. When did Alaska Junk first become steel jobbers?

A. Oh, we have been steel jobbers ever since I can remember. I would say we were steel jobbers from 1931, and probably a few years prior to that.

Q. Did Alaska Junk sell any scrap to any other concerns than the Oregon Steel people? Does it?

A. Oh, yes.

Q. What companies would there be?



(Testimony of Monte L. Wolf.)

A. The Bethlehem Steel in Seattle; we have sold in years gone by to the Northwest Steel Rolling Mills, which is located in Seattle.

Q. Are those the only two?

A. There have been times when scrap was hard to get, and [458] we have shipped east; I don't recall the names of the firms; but, basically, I would say that prior to the time we helped build the steel mill, we were agents of Bethlehem in this particular area, and we supplied 90 per cent of our steel scrap to them.

Q. Did you ever hear of any discussions among the partners, either at the office of the firm or at your home concerning the prospects for the sale of stock in Oregon Steel to outside interests?

A. Towards the latter part of 1943, from September on, yes, I did hear discussions.

Q. And what was the nature of those discussions?

A. Well, I know that Manuel Schnitzer and his mother were busy running over to Kaiser, and running over to Electric Steel and over to the plant. They were trying to interest Dulien from Dulien Steel Products. They got to the point where they could not operate the plant, and they couldn't let go of it, and they had to do something real fast.

Q. What kind of deal were they trying to work out with Dulien, if you know?

A. They were trying to work out a deal with Dulien that he would buy an interest in the mill.



(Testimony of Monte L. Wolf.)

Q. And that stock would be issued to him?

A. Yes, stock would be issued to him; and it even got to the point where they tried to sell the whole thing; because [459] it got to the point where they knew they could not swing it.

Q. And how much stock did they want Dulien to take?

A. My dad and the Schnitzers usually took care of those things themselves, and I didn't know too much of the details.

Q. Weren't you connected with the business at that time?

A. My part of the business consisted mostly of staying around the plant.

Q. What plant?

A. The Alaska Junk, or the warehouse, to see that our trucks were operating correctly, and to see that the shipping clerk was functioning properly, and the buying and selling; but when it came to the larger projects, I didn't know too much about them.

Q. You are the son of one of the major partners of the business, and you were actually associated with the business?

A. That's right.

Q. You say you cannot recollect any figure that was mentioned in connection with their interest?

A. I know the particular figure of \$125,000, and the stepping up of that figure from \$62,500.

Q. I am not asking about that. I am asking about any figures in connection with your desire for additional stock to be issued to outside parties.

(Testimony of Monte L. Wolf.)

A. No, I don't know what that would break down to; I know they wanted to sell the mill; and I knew we had a lot of [460] money that was tied up in accounts receivable and the mill.

Q. But here we are at a very crucial point in the development of this business of the Oregon Steel, in which both the Schnitzer family and the Wolf family have made tremendous advances, hundreds of thousands of dollars to the corporation, particularly in the form of advances,—partly in the form of advances of stock and partly in the form of these so-called advances that we have been discussing in the course of this trial. Now, there comes the crucial time when it looks as if you might lose a lot of money. Now, do you have any idea of what the figure was or what the amount of money was that they wanted to raise by way of stock issue at that time?

A. All I knew, when the corporation was formed they issued or were to issue \$250,000 worth of stock. But so far as how much money or the prices of the stock, I knew nothing about that, with the exception that at one time they told me,—they had a deal they had worked out with Kaiser for Kaiser to take the whole thing, and we would get our costs back. And then additional money was also tied up in other accounts which we had, accounts receivable, and I think it came to \$1,000,000.

Q. I am not talking about efforts to secure a purchaser for the mill. I am talking about your

(Testimony of Monte L. Wolf.)

efforts to secure funds from outside parties by the issuance of stock?

A. I cannot remember anything of that.

Q. Who else did they attempt to interest at that time, [461] at the end of 1943? Who else did they attempt to interest in the purchase of stock in the corporation besides Dulien?

A. I heard them talking about Barde from Barde Steel, and they contacted Mr. Woodbury from Woodbury and Company, and it seems to me there were some others. There were some people from the South, from somewhere in California, and I think they were supposed to send engineers to inspect the plant, because they were contemplating buying it. And then I heard when Kaiser was very much interested in the project, and then he got cold feet. Even though he wanted it, he could not come into the picture because it seemed that the steel corporations were very much against Kaiser taking it over, and then they lost interest and dropped out.

Q. When it was considered that additional stock in this corporation might be purchased by outside parties, what conversations do you remember concerning the relationship which would exist between the original interests, the old stockholders, and the new stockholders as to management and control and that sort of thing?

A. Well, I know they were constantly looking for capable people.

Q. I don't think you understand my question.

(Testimony of Monte L. Wolf.)

Just conceive the organization on the basis of the facts we have in the record; Morris Schnitzer and the Alaska Junk are the stockholders? [462]

A. Yes.

Q. It is their baby, so to speak? A. Yes.

Q. And there comes a time when it looks as if they are going to lose control unless they can raise some money, or sell some stock, and they attempt to raise new capital, from outside sources to be put into the organization. Now then from your knowledge of the business, you can readily conceive that a question comes as to what the terms,—

The Court: Cut out the argument and explanation, and go ahead and ask the question.

Q. (By Mr. Marcussen): There comes a time when the question of the amount of control,—

The Court: Ask him what they did. Counsel has spent five minutes making a speech which I do not want to hear. Just ask the question.

Q. (By Mr. Marcussen): What conversation took place concerning the relationship between the original stockholders and new stockholders that they were trying to interest to invest in the new enterprise, insofar as the control of the organization was concerned?

A. I believe the control of the organization,—Alaska Junk and Morris Schnitzer would try to keep control, even though they had to sell some of their own stock to attract new [463] capital, because I know they tried to make a deal; they went to



(Testimony of Monte L. Wolf.)

Dulien; they went to Woodbury; they went to those parties before they went to Mears and Hall; they tried to get each one to put in \$150,000, and tried to work it out so that they could get together enough working capital so that they could make a go of the mill. [464]

\* \* \*

### M. R. SCHNITZER

recalled as a witness by and on behalf of the Petitioner, having been previously sworn, was further examined and testified as follows:

#### Direct Examination

By Mr. Jones:

Q. You have already been sworn? A. Yes.

Q. You stated a rate of interest for borrowings for Alaska Junk on short term borrowings, 90-day notes at the First National Bank. You called me this morning to say that you made an error. Will you explain what it is.

A. I stated that the interest rate during the years I was there was 6 per cent, but last night I went down to the Alaska Junk and found out that in 1940, during the middle of the year, it was changed to 5 per cent. But prior to that it had been six.

Q. There is still some doubt in counsel's mind, or my mind, whether either of us asked you, Mr. Schnitzer, while you were on the stand, why the



(Testimony of M. R. Schnitzer.)

July entries on Exhibit 26, crediting the stock and debentures did not get recorded until July?

A. Yes, I testified as to that.

Q. Are you sure that you testified as to that?

A. Mr. Williams said I did. [466]

Q. Will you just state it, for the record, to be sure?

A. The stock and debentures were to have been issued as of either late November or early December, 1942. That was to have been done by Mr. Reilly, who was then our attorney. Mr. Reilly was in the habit of being somewhat slow because of the press of business, and he never did get all the certificates in in time. I never did see them, for that matter, and I called him up some time in July, and he told me that he had issued them, and then I made the entry.

The Court: That is exactly what you said yesterday.

The Witness: Yes.

#### Cross-Examination

By Mr. Marcussen:

Q. It is your understanding that the debentures were actually issued in accordance with the stipulation here, on January 12, 1943?

A. I don't know what the stipulation shows.

Mr. Jones: We stand on the stipulation.

The Witness: They may have been issued, but the discussion was, I believe, in early December.

Mr. Jones: We have stipulated that.

(Testimony of M. R. Schnitzer.)

The Witness: That was the basis on which they were shown on the books at the time.

Mr. Jones: There is no question about that.

Mr. Marcussen: That is all. [467]

Mr. Jones: Thank you.

The Court: You may stand aside.

(Witness excused.)

Mr. Jones: Now, Mr. Johnson, will you come forward and be sworn?

Whereupon

J. F. JOHNSON

called as a witness by and on behalf of the Petitioner, having been first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Jones:

Q. Will you state your name?

A. J. F. Johnson.

Q. What is your occupation?

A. Certified Public Accountant.

Q. How long have you been a Certified Public Accountant?

A. Since 1933.

Q. And who have you worked for?

A. I worked for Price-Waterhouse & Company from 1931 until 1942; from 1942 until 1944 I worked with the War Production Board, and since 1944 I have been associated with Mr. Robert T. Jacob and his associates.

The Court: Where?

(Testimony of J. F. Johnson.)

The Witness: In Portland. [468]

The Court: Has all your activity been in Portland?

The Witness: In Portland; in Oregon and Washington; generally in Oregon.

Q. (By Mr. Jones): What was your status or grade, or whatever Price-Waterhouse called?

A. I started as a Junior Accountant, and when I left I was a Senior Accountant.

Q. How long have you been a Senior Accountant? A. Approximately six years.

Q. Did you go to any schools to study accounting?

A. Yes; I went to the University of Oregon.

Q. Are you a graduate of that school?

A. I am.

Q. Are you a member of any accounting association?

A. I am a member of American Institute of Accountants, and the Oregon State Society of Certified Accountants.

Q. What has been the nature of your work while associated with Mr. Jacob?

A. I have done general work, analyzing accounts, and obtaining data for various purposes.

Q. What was the nature of your work with the War Production Board?

A. I was in charge of auditing work.

Q. I want to hand you an exhibit, I believe it is [469] Petitioner's 61, and I will ask you when

(Testimony of J. F. Johnson.)

and where was the first time you ever saw that (hands document to witness).

A. In the office of the Alaska Junk Company.

Q. What was the occasion for it to come to your observation there?

A. I was searching the tax files of the company in order to obtain data in connection with tax returns.

Q. Now, for all the other years we have the reports of the revenue agents on the four partners, but could you find those for Rose Schnitzer or Jennie Wolf or Sam Schnitzer for that year—what is it, 1940?

Mr. Marcussen: Yes.

Q. (By Mr. Jones): For the year 1940?

A. I was unable to find them in the file.

Q. Are these the only ones you found?

A. Yes.

Q. Did you make an inquiry about them.

A. Yes.

Q. Was a search made?

A. Yes; a search was made by the office manager at the time I inquired, and he was also unable to locate them.

Q. That is the reason they were not given to me?      A. That is right.

Mr. Marcussen: Do you know whether similar statements [470] were ever sent to the other partners of Alaska Junk?

A. I don't know; I have tried to find them.

(Testimony of J. F. Johnson.)

Q. (By Mr. Jones): You have made a search for them? A. Yes.

Mr. Jones: I might say that we do not know, but we assume there was some sort of a report for the year.

Q. (By Mr. Jones): Did you find anything for the year 1940?

A. Not for the other people.

Mr. Marcussen: Do you have any reason to believe that any statements were issued like this for the other partners?

The Witness: Well, only an assumption that, if they issued one to Mr. Wolf, they should have issued one to the others.

Mr. Marcussen: But you have never seen any?

The Witness: That's right.

Mr. Marcussen: And no one has ever told you there was such a document?

The Witness: That's right.

Q. (By Mr. Jones): We just never found any; is that right? A. That is right.

Mr. Jones: That is all I wanted to prove on that. [471]

Mr. Marcussen: You don't claim that any exists?

Mr. Jones: I don't know. I am just trying to account for not putting them in evidence, if there were not any.

Mr. Marcussen: I see.

Q. (By Mr. Jones): Have you ever done any accounting work for the Alaska Junk Company?



(Testimony of J. F. Johnson.)

A. Yes.

Q. And for how long?

A. For a period somewhat in excess of three and one half years, from time to time.

Q. I am going to hand you Exhibit 65 and ask you to state if you prepared this?

A. Yes, sir.

Q. I am speaking now of Exhibit 65?

A. That's right.

Q. From what sources did you make the preparation?

A. I prepared that from the accounts carried in the Alaska Junk Company ledger with the Oregon Electric Steel Rolling Mill.

The Court: He has not said what it was?

Mr. Marcussen: That is not in evidence; it is merely for identification.

Mr. Jones: Will you state what it is? [472]

The Witness: This is a summary of the Alaska Junk Company account with the Oregon Electric Steel Rolling Mills, as recorded in the Alaska Junk Company ledger.

The Court: For what period of time?

The Witness: For the period October 22, 1941, to November 25, 1943.

Q. (By Mr. Jones): It is a summary of this account here (indicating) which is Exhibit 26?

A. That is correct.

Mr. Jones: We offer Petitioner's 65 in evidence.

The Court: Just identified by the witness?

(Testimony of J. F. Johnson.)

Mr. Jones: Just identified.

The Court: All right, is there any objection?

Mr. Marcussen: No objection.

The Court: It will be admitted.

(The document referred to was marked and received in evidence as Petitioner's Exhibit No. 65.)

Q. (By Mr. Jones): Will you for the purpose of the record explain what that is?

The Court: I thought he had just done that.

Mr. Jones: I want him to tell what categories of accounts there are in it.

The Court: All right. [473]

Q. (By Mr. Jones): Go ahead.

A. It shows cash advances, debited, bills paid, and so forth. Merchandise furnished and debited, cash receipts debited, and debit balances.

Q. Will you state how much cash was advanced, the over-all total by the Alaska Junk to the Oregon Electric Steel Rolling Mills? A. \$327,870.23.

Q. And what was the amount of the bills incurred by Oregon Steel and paid by Alaska?

A. \$166,340.16.

Q. And what was the charge for the merchandise furnished by Alaska to Oregon Steel?

A. \$347,341.62.

Q. What amount of cash did Oregon Steel repay to Alaska?

A. The total credited by Alaska Junk on its records was \$114,519.88.

(Testimony of J. F. Johnson.)

Q. Why did you credit this on its records?

A. \$1000 was received, as I recall, from the Shaver Transportation Company,—

Q. Explain it fully.

A. And was credited by the Alaska Junk Company records to the Oregon Electric Steel Rolling Mills.

Q. How much does the account, Exhibit 26, show as the total [474] amount of money that Oregon Steel either paid directly to Alaska or that came into Alaska's hands from the Shaver Transportation Company, or whatever it was, and was credited on this account?      A. \$114,519.88.

Q. All right. What was the balance, the unpaid balance, as shown by the books of Alaska Junk Company on this account, Exhibit 26 on the 26th day of November, 1943?

A. On the opening of business on that date, it was \$428,132.13.

Q. What credits were made on that date on the account?

A. On November 26 there was a credit of \$142,200.33.

Q. And what do the books indicate that credit was for?

A. The explanation is "Our share in \$151,000 mortgage note issued in settlement of our open account and that of Morris Schnitzer, his share, \$8799.67. Payment on same terms as previous mortgage note of \$249,000; that is, \$15,100, with interest at 6 per cent, first payment 6/1/54."

(Testimony of J. F. Johnson.)

Mr. Jones: Counsel will stipulate that the mortgage referred to in this entry that was just read by the witness is the mortgage note which is described in the mortgage, Exhibit 24?

The Court: Does counsel for the Respondent agree to the statement which was just made by counsel by the Petitioner? [475]

Mr. Marcussen: It is so stipulated.

The Court: The record will so show.

Q. (By Mr. Jones): Now, the purpose of preparing Exhibit 65 was to indicate primarily what, Mr. Johnson? A. You mean Exhibit 65?

Q. Exhibit 65, yes.

A. It was prepared to indicate the nature of the charges on the books of the Alaska Junk Company.

Q. Broken down into what categories?

A. Into cash advances, bills paid, and so forth, and merchandise furnished.

Q. You said bills paid, and so forth. Could you give us a little more explanation of "and so forth"?

A. The "and so forth" applies to one item of approximately \$11,000 that Alaska Junk charged the Oregon Steel for cash apparently received direct by the rolling mill.

Q. This "and so forth," "bills paid, and so forth," does that refer to goods that they purchased and Alaska paid for?

A. The "bills paid" refers to that specifically

(Testimony of J. F. Johnson.)

and the "and so forth" is a qualification of that \$11,000 item.

Q. I see. I am now handing you a paper, and I will ask you to tell us what that paper (hands document to witness)?

A. This is a statement of settlement between the Alaska Junk Company and Morris Schnitzer, as at November 26, 1943. [476]

Q. Did you work this out? A. Yes.

Q. From what source?

A. The records of Alaska Junk Company, plus the aid of two Journal entries of the Oregon Electric Steel Rolling Mill.

The Court: Did the witness testify that he prepared the statement.

Mr. Jones: Yes, he did, Your Honor.

(The document referred to was marked as Petitioner's Exhibit No. 66 for identification.)

Q. (By Mr. Jones): Will you explain how you worked out this Exhibit No. 66?

A. The first item of the open account under the caption "Alaska Junk Company" refers to the balance on Exhibit 65 of \$428,132.13. The open account balance under the caption of "Morris Schnitzer doing business as Schnitzer Steel Products," shows \$26,493.77; that was determined from the Alaska Junk Company's journal entry shown on page 23 of the journal under date of December, 1943, plus a reference to the Oregon Electric Steel



(Testimony of J. F. Johnson.)

Rolling Mill's journal entry 3/20 and 3/21 of March 31, 1943. The total of the open account of the Alaska Junk Company and Morris Schnitzer amounts \$454,625.90.

Q. Does this show the pro-rating of the third mortgage [477] and note?

A. Yes; the third mortgage was pro-rated, \$142,200.33 to Alaska Junk, and \$8799.67 to Morris Schnitzer and that was pro-rated in proportion to the open account balance as shown on the line above, which I just mentioned.

Q. That left a balance of how much due Alaska Junk Company?

A. Due Alaska Junk Company at that point was \$285,931.80.

Q. And Morris Schnitzer?

A. \$17,694.10.

Q. When you say that left a balance, do you mean that after the \$151,000 were debited and credited as against the open balances?

A. Yes.

Q. And the balances that you mentioned were the balances left after that?

A. That is correct.

Q. There has been testimony in the evidence about a two-thirds and a one-third guarantee of the open accounts by Mr. Morris Schnitzer. Was that taken into account in working out the charge against Morris Schnitzer by the Alaska Junk, as shown by this Exhibit 66?

(Testimony of J. F. Johnson.)

A. That is correct.

Q. Will you explain how you worked that out?

A. My understanding is that liability for the guarantee [478] was two-thirds to Alaska Junk Company and one-third to Morris Schnitzer; there appears to be a slight miscalculation in the recording of this liability. As calculated it is \$202,350.60 for Alaska Junk Company and \$101,275.30 for Morris Schnitzer.

Q. What do those figures, the two figures mentioned, mean?

A. Those two figures are the respective liabilities per guarantee on the part of the Alaska Junk Company and Morris Schnitzer.

Q. For the combined balances?

A. That is right.

Q. In other words, that is the share under the guarantee argreement that was to be responsible for the combined balances? That is, the share of each?

A. That is correct.

Q. How did that leave Morris Schnitzer standing with respect to liability to the Alaska Junk Company?

A. The liability, as recorded, to the Alaska Junk Company was \$83,581.20.

Q. In other words, does that mean that under the guarantee the Alaska Junk Company had made, without this charge against Morris Schnitzer, would have been exceeded; that is, without the guarantee they would have borne a loss in excess of the figures

(Testimony of J. F. Johnson.)

you have given in the amount of \$83,581.20; that is, that much more than two-thirds of the loss? [479]

A. I am sorry, I didn't quite follow the question.

Mr. Jones: Will you read it, Mr. Reporter?

(Whereupon the last question was read aloud by the reporter as above recorded.)

A. That is right. The entire loss, or the indicated loss to Alaska without the guarantee would have been \$285,931.80 instead of \$202,350.60.

Q. (By Mr. Jones): Is there an entry on the account, Exhibit 26, showing that Morris Schnitzer was charged with the amount of his guarantee?

A. Yes.

Q. Where does that appear?

A. That appears on the back of page 74 of Exhibit 26.

Q. Then, starting again with the balance at the beginning of business on November 26, 1943, what was the amount of the balance due from Oregon Steel to Alaska?

A. Will you repeat that question?

Q. What was the amount of the balance due Oregon Steel from Alaska on November 26, 1943?

A. I think you have it reversed.

Q. What was the amount of the balance due from Oregon Steel to Alaska on November 26, 1943? Isn't that what I said?

A. No, I think you had it reversed.

Q. What is the answer? [480]

A. \$202,350.60.

(Testimony of J. F. Johnson.)

Q. At the beginning of business?

A. At the beginning of business on November 26?

Q. Yes.

A. I made a mistake. I beg your pardon. It was \$428,132.13.

Q. And then what credits were made that day on that balance?

A. A credit of \$142,200.33.

Q. And what credit was that?

A. That was for Alaska's share of the \$151,000 mortgage note.

Q. And what is the next credit?

A. And a credit of \$83,581.20 for the purpose of charging Morris Schnitzer with one-third of the total loss in the steel mill deal.

Q. That is what it says there in the notes, is it not?

A. That is right.

Q. And is that credit that you are talking about that was worked out on Exhibit 66 to show his liability under the guarantee?

A. Yes.

Q. And that left an unpaid balance on that date due Alaska Junk of what amount?

A. \$202,350.60. [481]

Q. Does the account show what was done with the unpaid balance?

A. Yes.

Q. Will you state it?

A. There is a subsequent journal entry which states "To transfer balance of account lost in settlement of account to bad debts."

(Testimony of J. F. Johnson.)

The Court: That language means that you charged \$202,350.60 as a bad debt; is that what you mean?

The Witness: That is right.

The Court: On what date?

The Witness: That entry was recorded on December 31, 1943.

Q. (By Mr. Jones): Now, can all the figures on Exhibit 66 be ascertained from Exhibit 26?

A. With the exception of the assistance of two steel mill journal entries, they can be.

Q. Can you, by making any subtraction from these amounts here, take the whole figures right off of this entry (indicating)? Isn't Morris Schnitzer's full liability stated in that entry?

A. It is necessary *to use* of these two other entries to arrive at Morris Schnitzer's open account.

Q. What entries are they? Are they listed here? [482]

A. They are the Oregon Steel mill entries 3/20 dated March 31, 1943.

Q. Are these the *journal that* you are referring to? There are four of them there (indicating)?

A. Two of these journal entries are the ones referred to.

Q. All right. Then, with the assistance of the journal entries, Exhibit 7, and the account, Exhibit 26,—is all the information found in those two exhibits from which this account is worked out? That is, I am referring to Exhibit 66?



(Testimony of J. F. Johnson.)

Mr. Marcussen: It is 65.

The Witness: 66 is correct.

Q. (By Mr. Jones): Exhibit 66, isn't it?

A. That is right.

Q. Now, what was the answer to my question: do you get all the information between these two exhibits, which are Exhibit 7 and Exhibit 26, from which the calculation on Exhibit 66 is made?

A. That is right, with the aid of those two entries mentioned.

The Court: Was the last exhibit offered in evidence?

Mr. Jones: I think at this time I will offer it in evidence.

Mr. Marcussen: No objection. [483]

The Court: What is the number?

Mr. Jones: 66.

The Court: Petitioner's 66 will be admitted in evidence.

(The document referred to, heretofore marked as Petitioner's Exhibit 66 for identification, was received in evidence as Petitioner's Exhibit 66.)

The Court: And that is what?

Mr. Jones: That is the settlement between the Alaska Junk Company and Morris Schnitzer as at November 26, 1943.

The Court: As shown by the statement prepared by the witness from the books?

(Testimony of J. F. Johnson.)

Mr. Jones: As prepared from documents in evidence.

(The document referred to was marked as Petitioner's Exhibit No. 67 for identification.)

\* \* \*

### Cross-Examination

By Mr. Marcussen:

Q. I hand you Exhibit 26, Mr. Johnson, and ask you to refer to the month of December, 1942, in that account.

A. All right.

Q. Will you refer to the last few days of December, 1942, on that account, and also the first few days of 1943? Do you have them there?

A. Yes.

Q. Now, within a range of from December 28 to January 3, will you give me approximately the highest balance in that account during that period? Have you found that, Mr. Johnson? A. Yes.

Q. What is the maximum balance and on what date?

A. The highest balance after posting of invoices is on January 8, 1943, and is \$578,588.86. However, I do note [488] that subsequent to that time there appears to be some additional items which are dated back to 1942.

Q. I am not going to ask you to make any adjustments now as to that account, but merely to testify as to what that account shows. Are the

(Testimony of J. F. Johnson.)

items entered in that account according to date on which the transactions actually occurred?

A. It appears in some instances there are items entered in here that are not in exact chronological order.

Q. Is it generally true that they are in there in chronological order?

A. Yes, I would say so.

Q. And with respect to those that are not in any chronological order, are they general entries or entries of substance?

A. Giving it a quick glance, at least looking at these sheets, I don't see any of any particular substance.

The Court: I didn't hear the answer.

The Witness: Just looking at these sheets, I don't see any of any particular substance that may be out of chronological order.

Q. (By Mr. Marcussen): Did you testify what the highest balance was? A. On January 8.

Q. I didn't ask about January 8. I asked you to embrace a period from December 28, 1942, to January 3, 1943.

A. I would say the highest balance was \$578,-588.86. [489]

Q. Now, how does that balance compare with the balance at any times during the period that I identified, generally?

A. From December 25, as I recall?

Q. What is the lowest figure?

A. The lowest?

(Testimony of J. F. Johnson.)

Q. Yes.

A. The lowest is \$370,576.65.

Q. And what date is that?

A. That is immediately following the entry on December 30, 1942.

Q. And what was the entry.

A. A credit to cash of \$12,820.10.

Q. That does not account for the entire difference. There is a difference of some \$200,000 or more, isn't there?

A. That is correct.

Q. What are those items?

A. On December 29, there is an entry from the disbursements record, page 117, First National Bank, \$100,781.25.

Q. What does the item show?

A. That shows payment to the First National Bank.

Q. Payment to the First National Bank?

A. Yes.

Q. By whom? A. Alaska Junk Company.

Q. That is the account of Oregon Electric on the books [490] of the Alaska Junk Company?

A. That is right.

Q. And that was not a payment to the bank, was it?

A. Yes, it was.

Q. Doesn't it represent a loan from the bank to Oregon Electric, on which Alaska Junk was liable as endorser or otherwise?

A. This entry represents a payment to the First National Bank by the Alaska Junk, and charged to the Oregon Electric Steel Rolling Mills.

(Testimony of J. F. Johnson.)

Q. On behalf of the Oregon Electric Steel?

A. That is right.

Q. What about the next entry? Is that a sum of \$100,000 on the same date?

A. That is right.

Q. Do you know the difference between the two items, and why they are stated separately?

A. Yes.

Q. What is the difference?

A. The first item is a payment covering four \$25,000 notes of Oregon Electric plus interest of \$781.25.

Q. And what is the second item?

A. The second item was a payment which, I believe, wound up with the Portland Branch of the Federal Reserve Bank.

The Court: We will take a seven minute recess. [491]

(Whereupon a seven-minute recess was taken.)

The Court: Does counsel for the Respondent desire to resume cross-examination?

Mr. Marcussen: If Your Honor please, I would like to excuse this witness. It is my understanding that the Petitioner plans to call Mr. Morris Schnitzer back to the stand again.

Mr. Jones: No; I am not going to call him.

Mr. Marcussen: And may the further cross-examination of this witness be postponed until further cross-examination of Mr. Morris Schnitzer?



(Testimony of J. F. Johnson.)

I am making that request in the interest of saving time.

The Court: I thought you had finished the cross-examination of Mr. Morris Schnitzer.

Mr. Marcussen: There are a couple of other items that I would like permission to interrogate him on, and then recall this witness for a question or two about entries on certain dates.

The Court: Is there any objection?

Mr. Jones: I have no objection.

The Court: All right. The witness will stand aside.

(Witness excused.)

Whereupon,

### MORRIS SCHNITZER

recalled as a witness by and on behalf of the Petitioner, having been previously sworn, was further examined and testified as follows:

#### Further Cross-Examination

By Mr. Marcussen:

Q. Mr. Schnitzer, there has been testimony here concerning a guarantee agreement that was made between you and the Alaska Junk Company, and there has been some doubt as to the approximate date that was entered into. Can you state when it was?

A. I couldn't tell you the exact date.

Q. What is your best recollection?

(Testimony of Morris Schnitzer.)

A. I couldn't tell you whether it was the last week or the last couple of days in December, or the first part of January. I personally think it was the last week of December, because at that time we made a standby agreement with the Reconstruction Finance Corporation, whereby we agreed, the Alaska Junk and I, to stand aside and give the Reconstruction Finance Corporation priority.

The Court: What year was that?

The Witness: December, 1942. I had to make this guarantee agreement on the insistence of Mr. Wolf. Whether it was the middle of December or not, I don't know; I couldn't tell you the exact date.

The Court: Is counsel for the Respondent ready to [493] proceed?

Mr. Marcussen: Yes; I have just handed counsel a document for his examination.

Q. (By Mr. Marcussen): Mr. Schnitzer, I hand you a file containing a letter, date March 18, 1943,—this is a copy, and it is addressed to the Reconstruction Finance Corporation, Washington, D. C., attention Mr. Morton MacCartney; it is a two page letter, and signed on behalf of the Oregon Electric Steel Rolling Mills by Morris Schnitzer; and I will ask you if you wrote that letter? A. Yes, I wrote that letter.

Mr. Marcussen: If Your Honor please, I would like to offer the letter in evidence for the purpose, among other things,—

(Testimony of Morris Schnitzer.)

The Court: What is the date of the letter?

Mr. Marcussen: It is dated March 18, 1943, and the part to which I particularly want to call his attention is contained on the second page; it is the second paragraph there, "We have cooperated and gone ahead against all obstacles, with which I am sure by now you are acquainted, and tried to do an honest job. In fact, we never originally intended to put in over (and it would not have been necessary) the \$500,000 we were supposed to put in as our share in the capital investment."

Mr. Jones: We object to that, on the grounds that [494] it is incompetent, irrelevant and immaterial, and obviously an expression of nothing more than an opinion in the matter, and it does not come right down and say what we did put in. It doesn't say what either Alaska Junk,—it does not refer to the Alaska Junk; it doesn't refer to anybody; it is not in any way tied in with the Alaska Junk.

The Court: I will overrule the objection.

Mr. Jones: May I have an exception.

The Court: Yes, an exception will be noted by the Petitioner, and the document just identified by the witness will be admitted as Respondent's AA.

(The document referred to was marked and received in evidence as Respondent's Exhibit AA.)

Mr. Marcussen: And may I ask permission to withdraw the exhibit and substitute copies?

The Court: That permission is granted.

(Testimony of Morris Schnitzer.)

Mr. Marcussen: I have no further questions about it.

Q. (By Mr. Marcussen): I call your attention to a letter dated December 23, 1942, addressed to William Kennedy, manager, Portland office, RFC, and executed by Oregon Electric Steel Rolling Mills by Morris Schnitzer, President, and ask you if that is your signature on that letter (hands document to witness)?

A. Yes. [495]

Mr. Marcussen: I offer that as Respondent's Exhibit next in order.

The Court: That is a copy of a letter just identified by the witness?

Mr. Marcussen: Yes.

The Court: Is there any objection?

Mr. Jones: No objection.

The Court: It will be admitted as Respondent's BB.

(The document referred to was marked and received in evidence as Respondent's Exhibit BB.)

Mr. Marcussen: I also ask leave to withdraw it and substitute a copy.

The Court: The permission will be granted.

Q. (By Mr. Marcussen): In the early part of the year 1943, who were the stockholders of the corporation?

The Court: I believe I will not permit you to go into that; that was gone into yesterday; there is

(Testimony of Morris Schnitzer.)

no use going over it again with each witness, or with the same witness.

Mr. Marcussen: I am just trying to ascertain,—

The Court: What do you want to ascertain? That was gone into at the beginning of the case; that has already been submitted in evidence. Go ahead with something that you have overlooked.

Mr. Marcussen: I would like to ask with respect to [496] the same period of time whether any efforts were made at that time to interest stockholders,—

Mr. Jones: That was gone into yesterday.

The Court: Very thoroughly, I think.

Mr. Marcussen: Very well, I have no further cross-examination.

The Court: Are there any questions?

Mr. Jones: Yes; one on this exhibit here.

### Redirect Examination

By Mr. Jones:

Q. Mr. Schnitzer, I will hand you Respondent's AA and ask you to direct your attention to the next to the last paragraph on page 2 (indicating). Look that over and please make any explanation of that paragraph that you like.

A. This \$500,000 referred to here was the \$250,000 actual capital, plus \$150,000 working capital plus the balance of raw material on which we made out the original pro forma working sheet on our original RFC loan request.

The Court: Were you reading from the letter?



(Testimony of Morris Schnitzer.)

Mr. Jones: Just read that part.

The Witness: "We have cooperated and gone ahead against all obstacles, with which I am sure by now you are familiar, and tried to do an honest job. In fact, we never originally intended to put in over (and it would not have been necessary) the \$500,000 we were supposed to put in as [497] our share of the capital investment. As of February 28, we had put in over \$700,000 of our own money, and we are having one devil of a time trying to get the monthly disbursements from the RFC. This disbursement now is at least 45 days behind time, and it is unfair to ask our contractors and suppliers to wait any longer for their money. We feel it as great an obligation on your side to disburse the money for this job as it is on our side to build and get this plant into production and to aid in the national defense program. We feel, too, that it should be unnecessary to delay paying these just bills when they are promptly due."

Q. (By Mr. Jones): That figure of \$500,000 that you mentioned in the beginning of this paragraph, "We never intended to put in over (and it would not have been necessary) the \$500,000 we were supposed to put in as our share of the capital investment." I want you to particularly explain what you meant in that sentence?

A. The original intention of the \$500,000 was a maximum of \$250,000 in capital stock, and we agreed in our pro forma or we intended in our pro

(Testimony of Morris Schnitzer.)

forma statement to advance \$150,000 in working capital and approximately in raw materials to help operate the plant.

Q. Did you expect the Alaska Junk Company to put in any part of that additional capital that went into the Oregon [498] Steel beyond the amount that they ultimately subscribed to?           A. No.

Mr. Jones: That is all.

#### Recross-Examination

By Mr. Marcussen:

Q. Who did you refer to by "we" in that letter?

A. The Oregon Steel.

Q. Who were "they"?

A. The corporation.

Q. Who did you mean by "we."

A. The stockholders and its officers.

#### Redirect Examination

By Mr. Jones:

Q. At which time you had 622 unissued shares, didn't you?           A. That's right.

Mr. Jones: That's all.

Mr. Marcussen: That's all.

The Court: You may stand aside.

(Witness excused.)

Mr. Jones: Mr. Grey.

Whereupon,

W. P. GREY

called as a witness by and on behalf of the Petitioner, having been first duly sworn, was examined and testified as follows: [499]

Direct Examination

By Mr. Jones:

Q. Will you state your name into the record?

A. W. P. Grey.

Q. Will you state what your occupation is?

A. Reporter for Dun and Bradstreet.

Q. How long have you been with Dun and Bradstreet? A. Sixteen years.

Q. What are your duties?

A. Gathering factual information regarding businesses and putting such information in the form of credit reports.

Q. And do you take care of those duties?

A. Yes.

Q. Where do you get your information? From what source?

A. Directly from statements given by the business men themselves, and from the records.

Q. Prior to your coming here, and the position that you held here, or have held here since your coming, was there any other person that occupied a similar position?

A. We have a good many reporters.

Q. Have you worked on the Alaska Junk Company reports?

(Testimony of W. P. Grey.)

A. I never worked on the Alaska Junk Company reports.

Q. Can you tell me where this report came from?

A. From the files of Dun and Bradstreet.

The Court: What do you mean by "this report"? [500]

Mr. Jones: I am not going to offer it in evidence. It is a report of Dun and Bradstreet.

The Court: It is a newspaper report?

Mr. Jones: No; it is a credit report on the Alaska Junk Company.

Q. (By Mr. Jones): Where did you obtain the report?

A. From the files of Dun and Bradstreet.

Q. Is this the official report on the Alaska Junk Company?      A. Yes. [501]

\* \* \*

The Court: Counsel for the Respondent is going to read into the record a portion of the Dun and Bradstreet report into the record, as I understand it?

Mr. Marcussen: Yes, from page 9-A.

Q. (By Mr. Marcussen): Is that properly identified?      A. Yes.

Mr. Marcussen: The last paragraph on the page I will read: "Of primary significance in the overall financial history of this business was the substantial altering of the financial condition during 1942 and 1943 arising from an investment in a business originally commenced as Oregon Electric Steel Rolling Mills. The latter company had been organ-

(Testimony of W. P. Grey.)

ized by Morris Schnitzer, son of Samuel and Rose Schnitzer, of the subject partnership. At December 31, 1942, advances from the predecessors to that former related concern totaled approximately \$572,000, such advances being subsequently extended to approximately \$75,000, of which \$125,000 was converted into common stock and approximately \$300,000 to 8 per cent debentures. The construction of the steel mill was finally completed during August, 1943, at a cost of over \$1,500,000, which was financed in a large measure through a commitment of \$700,000 from the Reconstruction Finance Corporation, secured [512] by a first mortgage and by an investment of the predecessor partnership. Active operations were commenced in August, 1943, but the mill was shut down late in October of that year for two primary reasons (1) cancellation of orders by customers and (2) lack of operating capital."

Q. (By Mr. Marcussen): Now, I want to call your attention to this sentence: "At December 31, 1942, advances from the predecessor to that former related concern totaled approximately \$572,000, such advances being subsequently extended to \$75,000." I will ask you whether the \$75,000 is an error, and whether that should not be \$750,000?

A. That I could not say without seeing the original notes. It might be or it might not be.

Q. Would you check the original notes to obtain that?



(Testimony of W. P. Grey.)

A. I would if I could find any report of them.

Q. What is meant by the term "predecessor to that former related concern"?

A. I did not write this report, and I knew very little about it except what we had in the file here.

Q. I won't take the time now. Will you read it and study it and be prepared to answer the question?

A. I couldn't tell you without reading the whole report.

Mr. Marcussen: If your Honor please, I would like to have the witness read the report, and ask him to be bound over [513] until this afternoon to explain that statement.

The Court: Does counsel have any objection?

Mr. Jones: That's all right.

The Court: All right. The witness will stand aside.

(Witness excused.) [514]

\* \* \*

Whereupon,

E. B. MacNAUGHTON

called as a witness by and on behalf of the Respondent, having been first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Marcussen:

Q. Will you state your name?

A. E. B. MacNaughton.

(Testimony of E. B. MacNaughton.)

Q. What position do you occupy?

A. Chairman of the Board of Directors of the First National Bank.

Q. Of Portland? A. Of Portland.

Q. Do you recall what your position was in the month of September, 1943?

A. I was President of the Bank.

Q. Now, Mr. MacNaughton, I hand you this file, which is the file of the First National Bank in respect to the Oregon Steel Mills, and I call your attention to a certain document contained therein dated September 4, 1943, identifying itself in the first paragraph as "Notes on a conference held Thursday, September 2, at 3:00 p.m. between EBM, Mr. Sam Schnitzer, Harry Wolf, and Mr. Lewellyn, plant manager, and the plant accountant in the offices of the Oregon Electric Steel Company." I ask you to state whether or not that is a correct identification of that document (hands document to witness)?

A. Yes.

Q. Who is EBM? A. That is myself.

Q. Will you kindly glance through that memorandum,— [526] by the way, was that prepared by you?

A. Yes.

Mr. Jones: What is the date of it?

Q. (By Mr. Marcussen): In the regular course of the bank's business?

A. Yes.

Q. Is that a correct memorandum of the facts it purports to recite?

A. It is.

Mr. Marcussen: Now, if your Honor please, in

(Testimony of E. B. MacNaughton.)

order to save time I would like to offer this memorandum in evidence.

Mr. Jones: I have not seen it yet.

Mr. Marcussen: Now, while counsel examines the memorandum, I would like to ask another question.

Q. (By Mr. Marcussen): What were your duties as President of the Bank, at that time, in 1943?

A. Being President of the Bank.

Q. Well, as such Bank President, what were your duties?

A. It was a full-time job; I was there every day, all the day. It was not an honorary title. We have a large bank with forty odd branches, and duties are delegated to department heads and branch managers and on questions of policy and questions of main credit lines I would enter into the discussions.

Q. Was this credit line a matter concerning which this memorandum contains a narration,—was that one of the important things that came to your attention?

A. It was at that time, yes.

Q. Now, I think reference is made in the memorandum to some of the causes of the failure, or, rather, financial embarrassment of Oregon Steel.

The Court: I think you had better wait until it is admitted before you examine the witness on the contents of it.

Mr. Marcussen: Very well, your Honor.

(Testimony of E. B. MacNaughton.)

The Court: As I understand it, this is a memorandum of the conference which took place?

The Witness: Yes.

The Court: Who were the parties involved?

The Witness: Alaska Junk and Oregon Electric Steel.

Mr. Marcussen: This was a conference between Harry Wolf, Sam Schnitzer and the bank.

The Court: What is the date?

Mr. Marcussen: September 2, 1943.

The Court: And that memorandum was made at the conference?

The Witness: Directly after the conference.

The Court: It is a report of the conference taken [528] from your files?

The Witness: It is a report of the conference which was made for our credit files.

Mr. Jones: Are you offering this in evidence?

Mr. Marcussen: Yes.

Mr. Jones: Have you had it marked?

Mr. Marcussen: No. Do you object?

Mr. Jones: I certainly do.

Mr. Marcussen: I will ask that it be marked.

The Clerk: Respondent's CC.

(The document referred to was marked for identification as Respondent's Exhibit CC.)

Mr. Jones: I will state my objection. We will object to it on the ground that it is incompetent, irrelevant and immaterial; it is a memorandum

(Testimony of E. B. MacNaughton.)

that Mr. MacNaughton has apparently made of some conference, and it does not go to dispute the testimony of any witness on the stand who has taken the stand here; it does not tend to dispute any fact that is stated in evidence by any of our witnesses, or any other witnesses who have testified. I cannot even comprehend the ground upon which counsel seeks to introduce it. If he states why he thinks it is admissible, I would like to have a chance to answer it.

The Court: All right. We will hear from Respondent's counsel. [529]

Mr. Marcussen: If your Honor please, this memorandum is a memorandum of a conference of the witness, who was the President of the First National Bank, who testified it was his custom to be called into the picture on the important credit lines, and this is a memorandum that he has prepared as to a conversation with Sam Schnitzer and Harry Wolf and Mr. Lewellyn, new plant manager, and the plant accountant in the office of the Oregon Electric Steel Company. It purports to deal with the credit position of the company at that time with reference to the RFC loan, and it purports to be based on the conference had with the Petitioners in this case, and, accordingly, it contains their admission, and it also covers the subject testified to by the witness, namely, the cause for failure of this mill; and also concerns the efforts that were made at the time by the Petitioners, Harry Wolf and Sam Schnitzer, concerning



(Testimony of E. B. MacNaughton.)

the disposition of the mill. There has been voluminous testimony in the case along that line.

The Court: I think this probably has some bearing on the question of the date and the transaction of the parties.

Mr. Jones: May I finish my objection before you rule, your Honor?

The Court: Certainly.

Mr. Jones: At the time that this was made, Mr. Morris Schnitzer was overseas, or was at least in the army. [530] This is dated September 4, 1943. There is a Mr. Schnitzer mentioned in here, and we have to assume from the heading of it that it is Mr. Sam Schnitzer.

Mr. Marcussen: You don't have to assume; it says it is Mr. Sam Schnitzer.

Mr. Jones: In the body of it, I am assuming that the Schnitzer mentioned there was Sam.

Mr. Marcussen: When references were made to Sam Schnitzer, of course it referred to him; the conference was with Mr. Schnitzer and Mr. Wolf, and of course it would be Mr. Schnitzer. Do you want me to further identify it?

Mr. Jones: You may identify it any way that you want to.

The Court: Who was present at that conference of which this purports to be a copy of what was said?

Mr. Marcussen: I will read it: Sam Schnitzer was there; Harry Wolf was there; Mr. Lewellyn,

(Testimony of E. B. MacNaughton.)

the new plant manager, and the plant accountant. I would like to ask counsel,——

Mr. Jones: Are you testifying?

Mr. Marcussen: You can look at it yourself and see; I am merely indicating what is shown on the memorandum.

Mr. Jones: Well, go ahead.

Mr. Marcussen: I would like to ask you, counsel, whether the plant accountant referred to there was Mr. Margosian? [531]

Mr. Jones: I don't know.

Mr. Marcussen: Mr. Margosian, were you in that conference?

Mr. Margosian: I don't remember.

The Court: Anyway, those are the ones that were named there?

The Witness: That is right.

The Court: Is the statement now being offered in evidence by counsel a correct statement of what was said and done by the parties?

The Witness: It is my version of what was said and done. There was a great deal of conversation, and, of course, it all wasn't taken down; but I put down what I thought was the pertinent part of the conversation, that related to the subject that was discussed.

The Court: That is what you understood?

The Witness: That is right.

The Court: And that is a correct report from your understanding?

(Testimony of E. B. MacNaughton.)

The Witness: As I heard it and as I understood it, I entered it at the moment.

Mr. Jones: Here is the heart of my objection. Now, there may be something about what Mr. Marcussen said in here, but I don't see it. It is a report of the discussion between Mr. Sam Schnitzer and Mr. Wolf and Mr. MacNaughton, and the whole document shows that Mr. Sam Schnitzer was in an irritable frame of mind, and about all it shows is his attitude.

The Witness: I will say that Mr. Schnitzer was constantly irritated at that time; it was not a temporary thing.

The Court: I will overrule the objection and receive the document in evidence. It is marked CC, as I understand it.

Mr. Marcussen: That is right.

(The document referred to, heretofore marked as Respondent's Exhibit CC for identification, was received in evidence as Respondent's Exhibit CC.)

Mr. Marcussen: I want to say that the only reason I want to offer the document is to save the witness going over the details, and I don't think it is necessary to do in view of the contents of the document itself. I would like permission to have a copy made so that this copy can remain in the bank's files.

The Court: Permission will be granted.

(Testimony of E. B. MacNaughton.)

Q. (By Mr. Marcussen): In evaluating credit risks, Mr. MacNaughton, can you state whether or not, from the point of view of the bank contemplating the making of a loan to a business, there is a greater risk in connection with making a loan to a new enterprise, with new management and inexperienced management, [533] as against an established concern with a record of earnings?

Mr. Jones: I think that is a matter calling for a conclusion of the witness;—

The Court: That is a conclusion that even the Court would know the answer to without being told.

Mr. Marcussen: I offer the witness as an expert.

The Court: You may answer the question.

A. Yes.

Q. (By Mr. Marcussen): The answer is that there is more risk in making a loan to a new enterprise under such conditions? A. Yes.

Q. A substantially greater risk, Mr. MacNaughton? A. Yes.

Q. Can you tell me, in the procedure of the bank and in the consideration it gives in granting loans, whether the bank gives any consideration in respect to the stock investments of the principal parties interested in the corporation?

A. In this case?

Q. Generally, in any case, and then later on I will ask you about this case.

A. In a new venture in which the participants



(Testimony of E. B. MacNaughton.)

are members of a firm which has been having business relations with the bank, we wrap everything there is in the organization back of the note.

The Court: Is that a matter of usual procedure?

The Witness: That is true in the banking business. We get everything, including the kitchen stove.

Q. (By Mr. Marcussen): That is in a new venture?

A. The same thing with more seasoned ventures, where there is trouble.

Q. Whether or not you are going to include the kitchen sink, does the matter of capital stock and the net worth enter into it?

A. Everything enters into it.

Q. What importance do you attach, for example, in an organization of \$2,000,000, I mean in a corporation having total assets of \$2,000,000,—what importance do you attach to the net capital and the net worth of the business in determining the line of credit that you would give the company?

Mr. Jones: That merely calls for something that is purely argumentative. It is wholly argumentative whether the capital ratio enters into it. We went into that argument with a witness yesterday, and I think it is wholly incompetent, irrelevant and immaterial, and we object to it.

The Court: Will you read the question, please?



(Testimony of E. B. MacNaughton.)

(Whereupon the last question was read aloud by the reporter as above recorded.)

A. We would give it a great deal of importance.

Mr. Jones: I have not had my objection ruled on.

Mr. Marcussen: It will be stipulated that the answer will be excluded until it is ruled on, if you insist.

The Court: It will be excluded until the answer is given. I will overrule the objection, and permit the answer to stand.

Q. (By Mr. Marcussen): What capital ratio do you ordinarily require, or would you like to see where you are granting what the bank would regard as a sound loan?

A. I don't know just how to answer that question. It depends on the risk, whether it is a new company or an old company, whether the principals are experienced in the business they are going into, and whether we feel they have a fighting chance in the field of competition.

The Court: I think you have gone far enough in that.

Mr. Marcussen: If your Honor please, this is a very important question to us.

The Court: Go ahead and ask the important question.

Mr. Marcussen: I submit this is important.

The Court: The trouble, counsel, is that you

(Testimony of E. B. MacNaughton.)

keep coming, and you don't get down to the real question. You spend too much time in preliminaries before you ask the question.

Mr. Marcussen: That question is a very important [536] one, and I would like to have your Honor rule.

The Court: I think he answered the question, I will ask the reporter to read it again.

(Whereupon the question referred to was read aloud by the reporter as follows: "What capital ratio do you ordinarily require or would you like to see where you are granting what the bank would regard as a sound loan?")

Mr. Jones: The First National Bank in the first place, did not make the mortgage. The RFC made the mortgage. All he is going into is a lot of theoretical economics.

The Court: I will sustain the objection.

Mr. Marcussen: Then, if your Honor please, I would like to make proffer of proof for the record, and have the record show that by this witness I seek to establish that the ratio of invested capital by the entrepreneurs in this business,—

Mr. Jones: Is this going in under rule?

Mr. Marcussen (Continuing): Or in any similar business should be in proportion, (1) to the total assets of such an organization, and (2) to their other fixed indebtedness, and (3) to the total indebtedness in a new venture with new man-

(Testimony of E. B. MacNaughton.)

agement, inexperienced in the steel business. May I have your Honor's ruling on that proffer?

The Court: The question was asked and the objection was sustained. Do you have any further question? [537]

Mr. Marcussen: Do I have a ruling on the proffer?

The Court: I sustained the objection to the question asked. If you have another question to ask, you may proceed to ask it. The Court is not going to permit counsel to show what he attempts to show; ask the question and the Court will rule on it. We will take a recess until 2:00 o'clock this afternoon.

(Whereupon the court recessed until 2:00 o'clock p.m. of the same day.) [538]

#### Afternoon Session—2:00 P.M.

The Court: Upon reflection, I feel that the Court erred once against the Petitioner and once against the Respondent as concerning the evidence which the Court permitted of statements made by the witnesses at a conference. I think the witness can testify what was said, but merely because it was reduced to writing, that does not give it any added weight or added validity; that will be reversed and the statement will be excluded; and the Court erred in not permitting questions to be propounded by Respondent's counsel before the recess.

Mr. Marcussen: May I have that exhibit please?

The Court: What was the number of that exhibit?

The Clerk: CC.

The Court: In order to identify that exhibit which the Court now excludes as Respondent's CC, unless counsel wants to ask the witness a few questions,—

Mr. Marcussen: I would like to ask the witness a few questions with respect to this conference. I simply want to ask the witness to refresh his recollection of this conference, to the extent that he can.

The Court: Can he refresh his recollection from the document?

Mr. Marcussen: Yes, I think I can ask him if that refreshes his recollection and whether he can testify to it; [539] Then, if he cannot do it, I will ask permission to introduce the document again.

The Court: We will rule on that when the time comes.

Mr. Marcussen: Just by way of anticipation, if your Honor please,—

The Court: All right, go ahead.

Whereupon,

E. B. MacNAUGHTON

resumed his testimony as follows:

Direct Examination

By Mr. Marcussen:

Q. Referring to the conversation you had with



(Testimony of E. B. MacNaughton.)

Sam Schnitzer, Harry Wolf and Mr. Lewellyn and the plant accountant, on September 2, 1943, Mr. MacNaughton, do you recall what was said to you at that time concerning——

The Court: I believe it might be well to show the purpose of the conference.

Mr. Marcussen: Yes, very well.

Q. (By Mr. Marcussen): What was the purpose of the conference? Do you recall?

A. Yes. Mr. Schnitzer,—Mr. Sam Schnitzer, Mr. Harry Wolf were long-time customers of our bank, and were prone to talk with me on numerous occasions about their troubles, and asked me to go down and look at the mill. We at the bank [540] were cognizant of the mill, its existence, although we were not financing it directly. They had gotten to the end of their rope financially; they were facing problems of marketing; they were in deep water; and they asked me to go down to look the thing over.

The Court: You mean by that, the mill?

The Witness: The rolling mill. They asked me to go down to see if I could get any information or give them any solace or advice; and, among other things, they wanted me to take an interest in the mill. I said that was out of the question. And out of that interview, I made these notations for our credit file, because while we were doing business with these men as partners and their wives, the loans which we made them were amply



(Testimony of E. B. MacNaughton.)

secured; nevertheless, we knew what was going into the mill venture, and unless that mill venture worked out, looking down the road something might happen in the *way revision* of their line of credit, and so forth.

Mr. Marcussen: Do you recall your conversation with them with respect to your putting capital into the enterprise?

The Witness: Yes.

Q. (By Mr. Marcussen): What did they say, as you can recollect it?

A. Well, they needed money. [541]

The Court: When you say "they," who do you mean?

The Witness: Mr. Schnitzer and Mr. Wolf. They needed money; and more money. They admitted that they needed someone to adjust the differences of opinion, because they were at wide variance in their attitudes toward this investment. Mr. Wolf was bitter about it, and Mr. Schnitzer was eager and optimistic about it. And for years I had been a sort of father confessor to them both, and they thought that if they could draw me into this thing I might adjust their variances of opinion. Also, they had come to realize as entrepreneurs in a business in which they had no previous experience, and confronting the market as it then prevailed, they wanted someone of a non-Semetic background who could front for the business. I might just as well get it out into the open; they

(Testimony of E. B. MacNaughton.)

wanted very much one of my sons to come into the business as a salesman or anything of that sort. They were deeply bothered and disturbed about where this thing was going to end for them.

Q. (By Mr. Marcussen): Now, with respect to the question about their overtures to you for an investment on your part, do you recall what the general substance of that conversation was?

A. They just asked if I would not consider going into that. I said it was impossible; I said I could not play on both sides of a business venture, while I was with the creditor [542] bank; while I was with a creditor bank I could not associate as an entrepreneur for an enterprise which, either directly or indirectly, we might be considered helping to finance.

Q. Was any figure mentioned as to the amount of stock they wanted you to take?

A. No. They just asked if I would consider it, and I said "no."

Q. Do you recall what was said during the course of that conference about the difficulty they were having in operation with respect, for example, to a Mr. Dawson?

A. Was he the superintendent before Mr. Lewellyn?

Q. Yes.

A. Yes; he had proved unsatisfactory to them, and had been replaced by a man named Lewellyn. These men had undertaken a business about which

(Testimony of E. B. MacNaughton.)

they knew little or nothing. The costs had gotten out of hand, and materials, particularly new materials and machinery, almost impossible to get; and they had to assemble cranes out of salvage material, or second hand material; and they had bought second-hand rolling mill machinery; and in those days when priorities were given to ship construction, and so forth, they had a heck of a time to put the thing together, and the costs had gotten out of hand. Also, they had gotten out of hand because they didn't know enough about the business, the engineering of it, to see that it went together properly; that is, to see that it [543] went together properly bit by bit.

Q. Now, with respect to the risk involved in investment in stock in an organization of that kind, which is a new venture, can you tell us about the degree of risk involved in such a situation?

Mr. Jones: If your Honor please, counsel has already gone into that.

The Court: I think so. He said a new business was more risky and more undesirable. I remember that. Get down to the specific question that you have in mind.

Q. (By Mr. Marcussen): In an organization of this kind,—I will rephrase that, please. In a going concern, an industrial concern, what, generally, from the point of view of sound financing,—and by sound financing, I mean financing by which the organization could reasonably expect,

(Testimony of E. B. MacNaughton.)

under normal conditions, not to be faced with financial embarrassment,—with that in mind, in a going concern, industrial concern, what ordinarily should be the ratio between the capital stock and net worth and the liabilities of such an enterprise?

Mr. Jones: If the Court please, that calls for purely a conclusion.

The Court: I know, but this witness is an expert. It is a matter of practice, I presume, with that banking institution, and I will overrule the objection.

Mr. Jones: I note an exception. [544]

The Court: An exception will be saved.

A. In a going concern the thing that the bank looks for is the ratio of assets to quick liabilities. As a general rule, there should be twice as much quick assets as liabilities; that ratio might change with the character of the business, for instance, if it is a wholesale grocery business, where the merchandise turnover is from twelve to fifteen times a year; in such cases we look at it quite differently. But, by and large, that is the ratio. And when that ratio becomes impaired through business management or due to the times, we begin to press for more security; instead of open credit we ask for secured credit in the way of inventory, or logs, booms, warehouse stocks, or what not.

Q. (By Mr. Marcussen): What ordinarily would be the ratio in a steel mill, bearing in mind the amount of money that must be in inventory,



(Testimony of E. B. MacNaughton.)

and the fact that it may take some time to get going?

A. We give them no credit except as we get secured credit on the supplies, such as scrap iron and the like.

Q. Generally, what would you say the current ratio should be?

A. You mean for the Bethlehem Steel, for instance?

Q. I mean this organization.

A. We didn't think they were entitled to any open line of credit. [545]

Q. I know, but what ratio would you think you would have to have required for a bank loan?

Mr. Jones: If the Court please, the witness has already said what he thinks, and besides, it is speculation.

The Court: I think he has already testified to it.

Mr. Marcussen: He has not answered it as it pertains to this enterprise.

The Court: I think you asked that in the preceding question, that they had no open line of credit.

Mr. Marcussen: I am asking him what the current ratio should be if he should make a loan to the concern unsecured.

The Court: He said they didn't have any open credit; I don't think we should ask him about something with respect to conditions that do not exist.

Mr. Marcussen: I am asking him as an expert.



(Testimony of E. B. MacNaughton.)

The Court: You have asked him as an expert, and he said the ratio should be 2 to 1 or better.

Mr. Marcussen: Very well.

Q. (By Mr. Marcussen): From the point of view of sound financing, what should be the ratio between the total capital and the net worth of the organization to its total liabilities, generally speaking?

A. Well, that is about the same as the question before. [546]

The Court: What is the answer?

A. I cannot give a definite answer; it depends on the business, the quality of the management and the current market conditions. That is a hard question to come down and give a definite answer on.

Q. (By Mr. Marcussen): Well, I am just asking you from the point of view of sound financing as I described it to you a moment ago, sound financing being such financing as would give the corporation or business involved money on a loan on a basis of a reasonable prospect of avoiding financial embarrassment under normal conditions?

The Court: Can you answer the question?

The Witness: I can only answer as a banker; I am not an investment banker; I am only a commercial banker.

The Court: Answer the question, if you can.

The Witness: I would say, as a commercial banker, with a loan against working capital you are talking about the ratio of investment capital to total assets or liabilities?

(Testimony of E. B. MacNaughton.)

Q. (By Mr. Marcussen): Yes.

A. We pay little attention to that; we look at the working capital on the ratios which pertain to it.

Q. Apart from the considerations solely as a commercial banker, do you know, generally, what the ratio should [547] be for the purpose of sound financing, as I have described it?

A. Sound mortgage financing or commercial bank financing?

Q. I mean, from the point of view of the corporation itself, the way it is set up.

A. I would rather not answer the question.

Q. By "rather not" you mean *do know* anything about that at all, Mr. MacNaughton?

A. It is such open ended question—the nature of the business and the nature of the management—

Q. You may make any qualifications or conditions which you like in order to give the answer.

A. Well, starting again, I will say I don't know.

Q. Do you recall anything that was discussed at that meeting concerning the unit costs of this plant?

A. Unit operating costs?

Q. Yes. A. No.

Q. That is, on the basis of per ton of steel?

A. No, I don't recall. Did I say something there (indicating document)?

Q. Yes. I will hand you this in a minute, Mr. MacNaughton. I call your attention to the second

(Testimony of E. B. MacNaughton.)

paragraph on the page (indicating), and I will ask you to read it.      A. Out loud? [548]

Q. No. And then I will ask you if that refreshes your recollection?      A. Yes.

Q. Does that refresh your recollection?

A. Yes.

Q. Could you testify concerning the question I asked you without referring to that now?

A. How is that?

Q. If I were to take the memorandum away from you could you answer the question?

A. What was the question that you wanted me to answer; if it is in dollars and cents, I would rather have it in my hand (indicating).

Q. You could not testify without having that in your hand?

A. I would rather refresh my recollections from it as I testify.

Q. I don't want you to read it and memorize it, but I just want to know whether, after reading it all, it comes back to your mind?      A. Yes.

Q. Does it?      A. Yes.

Q. Could you say what was said at the conference concerning the unit costs?

A. Mr. Lewellyn, who was the superintendent in charge [549] of operations, and Mr. Schnitzer and Mr. Wolf, said the bill of costs was running approximately \$38 a ton, which was out of line with the market and also the forecast which had been made for them by some cost accountant, namely that the

(Testimony of E. B. MacNaughton.)

price should not be more than \$31 a ton. It was also said that this \$38 a ton billing cost was high, because these costs were based upon the first runs and the plant had not been coordinated, and it had a good deal of frictional interference to get out of the way, and that they hoped to get the price down to the market level.

Q. What was the frictional interference that you referred to?

A. Well, in the commencement of operations in any plant there is always a period when new machinery and old machinery brought into the plant do not work together; there is a friction also which may come from differences of opinion between management and the foremen, or between management and the owners and stockholders; and there was a good deal of that in this business at that time.

Q. Do you recall the nature of the friction?

A. Well, I have indicated that one male partner, Mr. Wolf, was bitter about the whole speculative venture, and Mr. Schnitzer and his son had had differences of opinion growing out of the disappointment in costs, and so forth.

Q. You mean his son Morris? [550]

A. Yes. There got to be a time there when the two male partners would not talk to each other except through me or somebody else.

Q. You mean Mr. Sam Schnitzer and Mr. H. J. Wolf?

A. Yes.



(Testimony of E. B. MacNaughton.)

Q. What was the basis of Mr. Wolf's bitterness in these conversations?

Mr. Jones: I don't think that is material to any of the issues in this case.

Mr. Marcussen: It is very material, for this reason: There has been a lot of evidence introduced by the Petitioners to show it was one for all and all for one, and that this was a very fine cooperative venture, and there was a desire to limit the investment; and I think it has very great materiality.

The Court: I don't know what it is; it is a conversation between the parties about the very subject matter that the Court has to pass upon, so I will overrule the objection.

Q. (By Mr. Marcussen): Would you like to have the question read? A. Please.

Mr. Marcussen: Will you read it.

(Whereupon the question referred to was read aloud by the reporter as follows: "What was the basis of Mr. Wolf's bitterness in these conversations?") [551]

A. Well, Mr. Wolf was a man of a decidedly different temperament than Mr. Schnitzer. There were differences of opinion which naturally would grow out of that. Mr. Wolf was on the cautious side and Mr. Schnitzer was on the venturesome side; that was always true during their business experience; and I had known the gentlemen for a period of 35 years. When they went into this venture, at



(Testimony of E. B. MacNaughton.)

first the bank knew nothing about it, and then it appeared on the horizon, and as it merged above the horizon Mr. Wolf's cautiousness asserted itself and he knew it was something that neither one knew anything about, and he further said there was a concealment from him of the potentialities as to costs and as to hazards, and that he was being kept in the dark. On several occasions they came in and talked with me in the bank, and on numerous occasions, at least in the beginning, I told them that I thought they had made an unwise venture, out beyond their depth, that they had gone into a venture about which they knew nothing, and also without any basis as to the knowledge of costs. They were building it themselves without any expert supervision or control; in fact, that quality of management was almost impossible to get. In fact, the war industries had wiped out the market clean of anyone who had any knowledge of that kind of operation. They were feeling their way; Mr. Wolf was more and more concerned and was more and more bitter about it; and the bitterness was mutual, and as Mr. Wolf held [552] back Mr. Schnitzer became more and more restive; and it was an extremely difficult time for a partnership.

Q. I would like to ask you, in the course of those conversations, whom did Mr. Sam Schnitzer blame for the difficult circumstances that they found themselves in?

A. They blamed everybody from God down.

(Testimony of E. B. MacNaughton.)

Q. Can you identify any of these parties besides God?

A. Well, next to God came the bank. They thought we were too conservative; well, too bankish, that is all; and then, leaving the bank out of the picture, they began to criticize the superintendents they had and the machinations of the steel companies which they thought were blocking or interfering with them.

Q. Do you know whether there was anything to that or not?

A. I doubt it, because the steel companies had all they could do for the government without watching this small concern very much. And they got into family differences of opinion, and when they got into that I just closed my ears; and those two men, when they got to talking to each other, if it were not a tragedy, it would have been a comedy; it was Potash and Perlemuter, if you know what I mean.

Q. I call your attention to the last paragraph of this memorandum, and ask you to read that, and I will ask you if that refreshes your recollection as to any other matter as to [553] which Sam Schnitzer attributed the embarrassment at that time (hands document to witness)? I don't ask you to read it but ask you if that refreshes your recollection. Have you read it? A. Yes.

Q. Then I will ask you if you can testify without the memorandum? A. Yes.

Q. Will you go ahead.

(Testimony of E. B. MacNaughton.)

A. Well, Mr. Sam Schnitzer, who was the dominant moving spirit in this operation——

The Court: You mean in the mill operation?

The Witness: Yes. He especially criticized the former superintendent in charge of construction and operation, and also he was critical of his son, Morris, claiming that Morris more interested in buying second hand machinery at a bargain price than following out the plans of the original design. I will say this about Sam Schnitzer, that his continuity of thought was about as changeable as the New England weather; he would be for one program one week, and then he would be ready to start on something else the next; and it was just hell on wheels all the time they were trying to build that thing. While all that was going on, Harry Wolf was going around in the bank holding his hands to his head like this (indicating) saying, "My God, my God, where is it [554] going to end?"

Q. From your familiarity with the background of this organization and particularly with its organizers and the program it had laid out, and entirely apart from subsequent events, what, at that time, in your opinion, would be the prospect for success for such a venture?

Mr. Jones: That calls for a conclusion.

The Court: I don't think it would take an expert to prophesy about a situation of that kind.

Mr. Marcussen: Very well. Then I don't think testimony on that question would be required.

(Testimony of E. B. MacNaughton.)

Q. (By Mr. Marcussen): Now, from what you know about the background of the enterprise and the principals involved in it, can you state, from the point of view of sound financing, as I have already described it to you, what should be the ratio of the total capital contribution—capital stock and net worth to the total liabilities.

A. I have already answered that question.

The Court: He has answered it.

Q. (By Mr. Marcussen): You don't have any modification to make to your answer in the light the additional information that you have given the Court here?

A. As far as this venture was concerned, and viewing it as a banker, I would not have looked at the figures at all. [555] I would have looked at the quality of the ownership and the management it had, and written it off as a poor risk from the standpoint of banking credit. That is exactly what we did.

Q. Did the principals in this organization come to you or to the bank, rather, and request a loan in the early stages of its development?

A. For the rolling mill?

Q. Yes.

A. I don't think so. If they had they would have gotten a definite answer, "no."

Q. Did they come and ask you for a loan personally for the purpose of making an investment in the mill?



(Testimony of E. B. MacNaughton.)

A. We loaned them money, or had been loaning them money continuously for many years. As partners of the Alaska Junk Company they had a substantial net worth, and we extended them large credit, and they never misused it.

Q. Do you recall them asking you about a \$400,000 loan which they wanted you to put into the Oregon Steel Rolling Mills?

A. Specifically, I do not. These men were phenomenal successes as salvage merchandise dealers, starting at almost the pushcart level, and they had worked themselves up to be one of the most successful clients or customers the bank had; but going into this venture they went into waters about which they knew very little. [556]

Q. From the bank's files here I show you a memorandum dated April 15, 1942, bearing the initials at the end of AWG, and purporting to be a report on a conference with Mr. Sam Schnitzer and Morris Schnitzer and Mr. Groth. I will ask you to examine that memorandum, if you will, please (hands document to witness)?

A. Well, I have given it a quick glance.

Q. Does that refresh your recollection at all?

A. In a general way.

Q. As to any application for a loan by these stockholders in connection with the Oregon Rolling Mill?

A. Yes; the loan would come to them as individual partners; what they did with the money we had



(Testimony of E. B. MacNaughton.)

an interest in; and our loan was based on the Alaska Junk Company statement and their net worth.

Q. Do you know whether the application was made for a loan by Oregon Steel?

A. I couldn't answer that. Mr. Groth will have to answer that.

Q. Now then, after the organization was started, that is, the Oregon Steel, do you know whether any loans were made on secured credit?

A. By the bank?

Q. Yes.

A. We loaned them upon piles of scrap metal, on one or [557] two occasions, perhaps more.

Q. How about the accounts receivable?

A. And on the accounts receivable, also.

Q. Do you know anything about the details of this loan, or those loans, and the dates, and that sort of thing?

A. No; they were made in our branch downstairs, and that branch was in charge of Mr. Groth.

Mr. Marcussen: That is all, Your Honor.

### Cross-Examination

By Mr. Jones:

Q. Do you know whether or not the steel mill is working today? A. Yes, it is.

Q. Does it have an account with you people today, the First National Bank? A. Yes.

Q. I am calling your attention to this document in the file, and I will ask you to state what that is (hands document to witness)?

(Testimony of E. B. MacNaughton.)

A. This is a memorandum financial statement prepared by the bank's credit department, based upon financial statements submitted to the bank by the Oregon Steel Mills.

The Court: Of what date?

The Witness: As of the end of 1946—December 31, 1946, and December 31, 1947. [558]

Q. (By Mr. Jones): What does it show the capital stock of the steel mill to be?

Mr. Marcussen: An objection, if Your Honor please, on the ground that this is 1946, three years after the pertinent date.

The Court: I don't see the materiality.

Mr. Jones: The materiality is—he is arguing about a ratio, a ratio of assets to liabilities, and this definitely shows that the ratio——

The Court: All right, I will admit it.

A. \$187,800.

Q. (By Mr. Jones): Is that the unissued capital stock?

A. That is the outstanding capital for both years. It is identical.

Mr. Marcussen: I object on the further ground, it is already in evidence.

The Court: This is cross-examination of the witness.

Q. (By Mr. Jones): Does the statement show whether the company has any earned surplus?

A. Yes.

Q. What was the earned surplus for the year 1946? A. \$379,568. [559]

(Testimony of E. B. MacNaughton.)

Q. And for the year 1947? A. \$1,191,501.

Mr. Marcussen: Just a minute. Let the record show my objection.

Mr. Jones: I have not finished my cross-examination.

Q. (By Mr. Jones): In your experience with Mr. Sam Schnitzer, when something was going wrong, wasn't it true that it was his nature to place the blame rather indiscriminately?

Mr. Marcussen: I will object to that, if Your Honor please, on the ground that it calls for a conclusion of the witness.

The Court: I will overrule the objection.

The Witness: Shall I answer?

Mr. Jones: Yes.

A. Yes.

Q. (By Mr. Jones): Whether or not Morris Schnitzer was at fault or not, if Sam Schnitzer happened to be irritated at the time, it would be like him to place some blame on Morris?

Mr. Marcussen: I will object to that as not competent.

The Court: Let us not go into the details. I will sustain the objection to that.

The Witness: May I make a statement?

Q. (By Mr. Jones): Yes. [560]

A. Mr. Schnitzer would blame everybody but himself.

Q. Referring again to the balance sheet which you had in your hands a moment ago, that was

(Testimony of E. B. MacNaughton.)

submitted to you by the Oregon Steel Rolling Mill for your credit files, what are the total liabilities as shown for 1946 and 1947?

A. Current liabilities?

Q. No; the total.

A. Here is a total of \$1,248,450 for 1946.

Q. And for 1947?                      A. \$1,192,379.

Q. That is indicated on the statement as the total debts?                      A. Right.

Q. That, of course, does not include the liability for either stock or earned surplus?                      A. No.

Q. Are you acting as bankers for this firm?

A. The rolling mills?

Q. Yes.                      A. Yes.

Q. Are they operating successfully?

A. Yes.

Q. You have no information of your own as to whether any of the charges made by Mr. Sam Schnitzer against any of the [561] acts of Morris Schnitzer were true or false, did you?

A. No, sir.

Mr. Jones: That is all. Thank you very much.

The Court: Are there any further questions?

Mr. Marcussen: Yes, Your Honor.

### Redirect Examination

By Mr. Marcussen:

Q. I hand you file there, and call your attention to the balance sheet concerning which you have testified on cross-examination, and I will ask you

(Testimony of E. B. MacNaughton.)

whether it is true, as counsel stated, there is any item there identifiable as earned surplus?

A. It is designated solely as "surplus," but the difference between the surplus of 12/31/46 and 12/31/47 was earned surplus as between those two years.

Q. Doesn't it show a figure for surplus at the end of 1946 as compared with 1947—strike that. Doesn't it show about \$379,000 for the year end in 1947, and about \$248,000 for the year 1946?

A. You have missed the \$1,000,000.

Q. From what you know about surplus accounts, and so forth, is there any other way that could be increased besides by earnings to the corporation?

A. It could be contributed by stockholders or anyone else who wanted to put money into it; but they would be contributing [562] money and getting nothing for it.

Q. If a stockholder did it, it would increase the value of the shares?

A. Yes; it would be an increase in the net value of his shares. That is what you mean?

Q. Yes.

A. But on his books he would have an increased investment in the business.

Q. Precisely. Do you know whether this item of surplus included any items of paid-in surplus?

A. By the stockholders?

Q. Yes. A. No, it does not.



(Testimony of E. B. MacNaughton.)

Q. Or paid in surplus by the stockholders or resulting from any other means? A. No.

Mr. Marcussen: That is all.

Recross-Examination

By Mr. Jones:

Q. Your answer to the last question means that it does not represent any contributions, but represents earnings of the company?

A. It is the result of the earnings of the company. [563]

Redirect Examination

By Mr. Marcussen:

Q. Do you mean by that, that you know the increase in the years from 1946 to 1947 represents an increase in the accounts due solely to earnings?

A. That is right.

Q. You don't know what the \$379,000 was composed of as it stood at the end of the year 1946?

A. That is capital stock?

Q. You don't know whether that surplus came from earnings or what? You don't know where that surplus came from?

A. I couldn't answer that without seeing a statement for the year ahead.

The Court: Does counsel for the Petitioner want to ask any more questions?

Mr. Jones: No; thank you.

The Court: All right. You are excused.

(Witness excused.)

Mr. Marcussen: I will call Mr. Groth.

The Court: Is this another one of the Respondent witnesses?

Mr. Marcussen: Yes.

The Court: And this is by permission of counsel?

Mr. Jones: That is right.

Whereupon,

ARNOLD W. GROTH

called as a witness by and on behalf of the Respondent, [564] having been first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Marcussen:

Q. Will you please state your name?

A. Arnold W. Groth.

Q. What is your business or profession?

A. Vice President of the First National Bank of Portland; prior to Februry, I was manager of the main branch, also Vice President.

The Court: Prior to February of what year.

The Witness: This year, sir.

Q. (By Mr. Marcussen): Now, how long were you in the main branch of the bank?

A. I have been connected with the bank since 1921; and I have been connected with the main branch practically all of that time. That will need a little explanation. After 1927 we had a sort of redesignation of the departments, and at that time I became assistant manager of the main branch, and then was later made manager of the main branch.

(Testimony of Arnold W. Groth.)

Q. When did you become manager of the main branch?      A. About ten years ago.

Q. As manager of the main branch, will you state in a general way what your duties [565] were?

A. Well, the general management of the bank; particularly the responsibility for the loaning of its money in the main branch.

Q. Can you state whether or not an application was made by Oregon Steel—by the way, when we speak of “Oregon Steel,” that is just short for “Oregon Electric Steel Rolling Mill.”

A. I understand.

Q. Can you state whether an application was made for a loan in the amount of \$400,000 by Oregon Steel in connection with an RFC loan?

A. I would have to refresh my memory by looking at the files.

The Court: We will take a five minute recess.

(Whereupon a five minute recess was taken.)

The Court: I think we might save time if the witness has to check some matters to refresh his memory, while he is doing that to resume the testimony by Petitioner.

(Witness excused.)

Mr. Jones: Mr. Johnson, please.

The Court: The reporter will note that Mr. Johnson is recalled by the Petitioner.

Whereupon,

J. F. JOHNSON

recalled as a witness by and on behalf of the Petitioners, having been previously sworn, was further examined and [566] testified as follows:

Mr. Jones: We are going to stipulate into the record, subject to check for inaccuracies, the total amount of cash advances on Exhibits 41 through 55, and then the total cash repayment by the debtor back to the Alaska Junk.

The Court: 41 through 55? Are those Exhibits introduced for identification purposes?

Mr. Jones: They were just for identification; not offered.

The Court: These cash payments relate to collateral loans or other loans made?

Mr. Jones: That's right. I will have the witness do most of the dictating of the stipulation, and we will have it in here this afternoon.

The Court: All right, if that will save time.

#### Redirect Examination

By Mr. Jones:

Q. Have you got the figures with you?

A. Yes.

Mr. Jones: That is all.

(Witness excused.)

Mr. Marcussen: At this time I would like to call Mr. Margosian for further cross-examination.

Whereupon,

LEON D. MARGOSIAN

recalled as a witness by and on behalf of the Petitioner, having been previously sworn, was further examined and testified as follows:

Cross-Examination

The Court: You were sworn yesterday?

The Witness: Yes.

By Mr. Marcussen:

Q. Now, Mr. Margosian, I think yesterday you may recall that we discussed the questions of advances of stockholders to Oregon Steel? Do you recall that? A. Yes.

Q. I don't think it is necessary for me to recall your direct testimony or your cross examination. Do you remember it pretty well?

A. The general substance of it, sir, yes.

The Court: Without repeating what was said more than once, let counsel make the preliminary statement and get to the point, because we have to get through with this case sometime today.

Q. (By Mr. Marcussen): I asked you to produce accounting authorities which you had referred to in the course of your direct examination which would justify the practice which you described as good accounting procedure of listing advances to stockholders as a separate item outside of current liabilities, even though [568] they constitute current liabilities. Now, I would like to ask you to refer to the authorities which you have brought with you?



(Testimony of Leon D. Margosian.)

A. I would like to make a correction to that; I said that these were not all current liabilities. I would like to refer to the incidents leading up to the balance sheet's present condition. These vouchers or invoices from Alaska Junk Company came to the Oregon Steel mills in the same manner as all other vendors' invoices; we processed them in exactly the same way; we presented them to the Reconstruction Finance Corporation for payment along with other regular invoices; some of them were approved and paid. Those that were not approved and paid, we showed in accounts payable. Now, it was my understanding from the owners of the company that these accounts were to be paid either by the RFC or out of operating profits. I might say that a simple calculation would show me it would be more than one year before the entire amount of the indebtedness was paid off, assuming that the corporation got into active production immediately. It would only be a flight of imagination to imagine what part of this indebtedness would be paid during the next year, and, naturally, on account of that I could not put an indefinite amount under "current liabilities," so I showed the entire amount below the "current liabilities."

Q. It is your statement that yesterday you did not [569] characterize them as current liabilities?

A. They were current liabilities when they came in.

(Testimony of Leon D. Margosian.)

Q. What is your authority for the statement?  
What is the basis for the statement?

A. I was instructed by the owners of the firm and by Mr. Reilly, their deceased accountant, that after my entry for the stock issued and the debentures had been placed on the books, all other amounts would be current and would be paid either out of the RFC funds or operating profits.

Q. Now, I hand you Exhibit 17, and ask you whether that is the account of the Alaska Junk on the books of Oregon Steel (hands document to witness)?

A. Yes, sir.

Q. Is there anything on that that shows that that is an account payable?

A. Not on this ledger sheet.

Q. And did you establish that ledger?

A. Yes, I made it up.

Q. You did not indicate on there at all that this is an account payable?

A. Not on this ledger sheet.

Q. This is a copy from the books of the corporation itself which you were in charge of at the time?

A. Yes, sir.

Q. Now then, have you finished with the explanation [570] that you wanted to make in response to the question I asked you?

A. How is that?

Q. Have you finished with the explanation?

A. Yes.

Q. Now then, I want to refer to these authori-

(Testimony of Leon D. Margosian.)

ties that you brought here, and ask you to point out the passages in them which approve of the practices that I described in my original question that I asked you.

A. The first situation is the balance sheet's present condition of account.

The Court: What is that from?

The Witness: From "Auditing Theory and Practice" by Robert H. Montgomery.

The Court: What page are you reading from?

The Witness: 294.

Mr. Jones: What edition?

The Witness: 1940. The heading of this chapter is "Balance Sheet Present Condition of Accounts Payable."

Q. (By Mr. Marcussen): Is that the heading of the chapter, or simply a subheading to the heading?

A. A subheading. The second paragraph of this heading is as follows: "The term 'notes payable' may be used as a general caption under which may be listed separately items [571] such as trade indebtedness, advances to officers, dealers' deposits, etc. Amounts payable to affiliated companies should be stated separately."

The Court: Is that in quote?

The Witness: Yes. Now, my second quotation—

The Court: From what page?

The Witness: Page 286 of the same volume. The heading of the subheading is "Current Liabilities—

(Testimony of Leon D. Margosian.)

Definition and Classification.” “Obligations, the maturity of which will not extend beyond one year from the date of the balance sheet are current liabilities.” Now, manifestly, under this definition I could not place this particular account under “current liabilities.”

Q. (By Mr. Marcussen): Could you describe it as a current liability yesterday?

A. At the time it came into the office, yes.

Q. You described it here in court, referring to the items of advances to stockholders on the balance sheet Petitioner's 19, being the balance sheet dated October 31, 1941, for Oregon Steel—you stated the item there appearing as “advances from stockholders” in the amount of some \$450,000, as a current liability.

A. I should have made the qualification.

Q. They were not current liabilities, were they, then? [572]

A. As I say, the nature of these liabilities changed in my opinion, after they came into the office, and the payment of them was refused by the RFC.

Q. Referring to page 286. Was that the second quotation that you made from this book?

A. Yes.

Q. Did you read the preceding part of that chapter? A. Yes.

Q. I call your attention to the first page. I call your attention to the first page of the chapter which



(Testimony of Leon D. Margosian.)

is entitled "Current Liabilities," Chapter 15, and ask you whether you read that and up through to the next page about which you testified, page 286 (hands document to witness)?       A. Yes.

Q. Now, so that the record may be clear and your Honor will understand what I am interrogating the witness about, I would like to read, "Because most liabilities are fixed and definite in amount, opinion does not play such an important part in the determination of the amounts at which liabilities should be stated. The accounts receivable believed to be good may be paid, but the entire amount of the accounts payable in a going business must be paid in full. The chief difficulty regarding direct liabilities frequently lies in the ascertainment of their existence rather than in the determination of their exact amount." [273]

And then a heading "Distinction Between Liabilities and Capital." "Generally speaking, three classes of items are found on the credit or right hand side of the balance sheet: (1) liabilities; (2) capital; and (3) items which, in whole or in part are liabilities or capital, according to the circumstances. Examples of credit balances which normally would appear as liabilities but which under certain conditions are analogous to capital are the following: debts to stockholders which may be specifically subordinated to the claims of all other creditors and securities which appear on their face to be debts and which are so restricted in legal



(Testimony of Leon D. Margosian.)

remedies, that the holders thereof, in case of bankruptcy of the issuing corporation may rank with the stockholders rather than the creditors. The description which appears on a balance sheet as to securities such as are referred to, might read: 'twenty-year five per cent debentures due August 1, 1950, subordinate in every respect in event of liquidation to claims of other creditors.' Assessments paid by stockholders, although carried on the corporation's books as loans payable may be held to be capital if the facts disprove the entires on the books."

Did you have that passage in mind when you testified yesterday?      A. Naturally not.

Q. You did not?      A. No, sir. [574]

Q. If there is any conflict between that statement in the book and your testimony of yesterday, as an accountant, Mr. Margosian, would you have any comment to make upon it?

A. Would you repeat that question again, please?

Mr. Marcussen: Will you read the question, Mr. Reporter?

(Whereupon the last question was read aloud by the reporter as above recorded.)

A. Will you please explain that a little further?

Q. (By Mr. Marcussen): Yes, I will restate the question. As between the statement and your testimony, is there any conflict between what you said and what is stated in the book?

(Testimony of Leon D. Margosian.)

A. Sir, at the time I was making these entries, I was acting as accountant for the Oregon Steel. I was making the entries in good faith based on the knowledge which I had at the time and the information which I received from the owners.

Q. Let it be understood, Mr. Margosian, there isn't any question of your good faith now, but I am just directing your attention to what appears, to me at least, to be an inconsistency in the statement which I read from the authority which you have produced, and the testimony which you gave yesterday. Now, if there is any inconsistency, who do you say should be correct?

A. Under the circumstances which prevailed at the [575] time, at the time I made the entries, the assignments I made of the items was, in my opinion, correct.

Q. Do you think it is correct in the light of the statement which is read from the authority?

A. According to the conditions which I understood at the time, they are correct.

Mr. Marcussen: I think the record speaks for itself. I have no further cross-examination, except that I wish to further identify this volume by stating to your Honor that this is "Auditing Theory and Practice" by Montgomery, Sixth Edition, Ronald Press Company of New York, and apparently it is the second printing in December, 1940.

The Court: Is that all?

Mr. Marcussen: Yes.

(Testimony of Leon D. Margosian.)

Mr. Jones: The witness says he has one other thing that he wants to bring before the court with respect to his authority.

The Witness: This bulletin is entitled "Examination of Financial Statements by Independent Public Accountants." It was issued in January, 1936, by the American Institute of Accountants.

Q. (By Mr. Marcussen): What is the name?

A. "Examination of Financial Statements by Independent Public Accountants." [576]

The Court: Who is the author of the book?

The Witness: It is a bulletin prepared and published by the American Institute of Accountants.

The Court: What date?

The Witness: January, 1936.

The Court: You want to read something from that?

The Witness: Just one excerpt. On page 24, under the title of "Accounts Payable," and sub-heading No. 5: "Liabilities to affiliated companies and advances by stockholders, directors, officers and employees, if material in amount should be shown separately on the balance sheet."

The Court: Does that complete the reading?

The Witness: Yes.

Q. (By Mr. Marcussen): Is there anything in this book——

The Court: You mean the document from which he has just quoted?

Mr. Marcussen: Yes.

(Testimony of Leon D. Margosian.)

Q. (By Mr. Marcussen): —which justifies the practice of stating those advances outside of the caption of “current liabilities,” if, as a matter of fact, they actually consist of current liabilities?

A. I explained that.

Q. I just want you to answer the question. [577]

The Court: Just give your answer.

Q. (By Mr. Marcussen): What is your answer to that question? I have permitted you to give every explanation you desire, but I don't think you have answered that question.

A. Will you read the question, please?

Mr. Marcussen: Will you repeat the question, Mr. Reporter? I believe it was stated in two sections.

(Whereupon the question referred to was read aloud by the reporter as follows: “Is there anything in the book which justifies the practice of stating those advances outside of the caption of ‘current liabilities,’ if, as a matter of fact, they actually consist of current liabilities?”)

Q. (By Mr. Marcussen): You can answer yes or no to that question.

A. Not in that particular booklet.

Q. Is there in any particular booklet?

A. By the same organization?

The Court: The Court is not going to tolerate any more questions about any more books.



Mr. Marcussen: Very well.

The Court: The witness is excused.

(Witness excused.)

Mr. Marcussen: We have a stipulation which I think will save time, if you will give us a few moments? [578]

The Court: All right. We will take a short recess.

(Whereupon a short recess was taken.)

Mr. Jones: I will call Mr. Johnson back to the stand.

Whereupon,

**J. F. JOHNSON**

recalled as a witness by and on behalf of the Petitioner, having been previously sworn, was further examined and testified as follows:

**Direct Examination**

By Mr. Jones:

Q. I am handing you Exhibit 41 for identification, Mr. Johnson, and as a preliminary question, I will hand you all the Exhibits 41 to 55 inclusive, and ask you if you have calculated all the cash advances made by Alaska Junk Company to all the persons named on these accounts, Exhibits 44 to 55—41 to 55? A. I have.

Q. Have you also ran a debit on all the cash payments on these accounts, or the cash collections?

A. Yes.



(Testimony of J. F. Johnson.)

Q. Or the cash collections which have been made by the Alaska Junk Company from the persons named as debtors in the accounts?

A. That is right; cash collected by the Alaska Junk [579] Company.

Q. Have you got the total of all those with you here? A. Yes.

Q. Will you refer to your notes from the National Machinery account?

A. The National Machinery Company, cash advances \$1732.31.

Q. How much repayment was there to the Alaska Junk Company from the National Machinery Company?

A. Cash collections, \$47,099.55.

Q. Take Exhibit 42 for identification, Central Supply; how much money was advanced by Alaska? A. \$15,500.

Q. All right. During the period shown by this account No. 42, or Exhibit 42, how much in cash was repaid? A. \$104,968.27.

Q. That is, repaid by Central Supply to Alaska?

A. That is correct.

Q. Take Exhibit 43, Schnitzer Steel Products Company. How much cash was advanced by Alaska Junk Company to the Schnitzer Steel Products?

A. \$119,020.99.

Q. And how much cash was paid to Schnitzer Steel Products—by Schnitzer Steel Products to Alaska Junk Company? A. \$17,517.37. [580]

(Testimony of J. F. Johnson.)

Q. Take the Carlton and Coast venture, Petitioner's 44 for identification. How much money does that account show the Alaska Junk Company advanced to Carlton and Coast? A. \$27,525.

Q. And how much does the account show that Carlton and Coast repaid Alaska Junk?

A. \$134,649.94.

Q. Take Petitioner's 45 for identification, which is the Marshfield Bargain House account. How much does the account show that the Alaska Junk advanced to the Bargain House in cash?

A. \$4500.

Q. How much does the account show the Bargain House repaid to Alaska Junk?

A. \$6289.44.

Q. Let us take the Vaughn Motor Works, Exhibit 46 for identification. How much does the account show the Alaska Junk advanced?

A. \$2225.

Q. How much does it show the Vaughn Motor Works repaid Alaska Junk? A. \$746.34.

Q. Take Exhibit 47 for identification, Industrial Air Products Company. How much does the account show that Alaska Junk advanced to Industrial Air Products? [581] A. \$94,427.03

Q. How much does the account show the Industrial Air Products repaid to Alaska?

A. \$35,430.70.

Q. Take Exhibit 48, M. Turn, how much does

(Testimony of J. F. Johnson.)

Exhibit 48 for identification show that the Alaska advanced to M. Turn?      A. \$1600.

Q. How much does the account show was repaid?      A. \$300.10.

Q. Take "Cash Advances on Scrap" General Accounts, Petitioner's 49 for identification. What does it show the total of the cash advances by the Alaska Junk to the various people named on that accounts totals?      A. \$1971.08.

Q. Does it show any cash repayments?

A. Yes, sir.

Q. What is the amount?      A. \$1457.84

Q. Take Exhibit 50, Munce and Pedrante, Petitioner's Exhibit 50. Did the Alaska Junk advance any amounts to Munce and Pedrante during the period covered by the account?      A. Yes.

Q. How much?      A. \$4479.63.

Q. How much did it receive back from Munce and Pedrante [582] in cash payments?

A. \$2148.51.

Q. Take Emil Nyberg, Petitioner's 51 for identification. How much does this account show the Alaska Junk Company advanced Emil Nyberg?

A. \$2750.

Q. Does it show any cash repayments by Nyberg to Alaska?

A. May I see the ledger sheet (indicating)?

Q. All right. (Hands document to witness.)

A. None.

Q. Take the case of R. Pedrante, Petitioner's

(Testimony of J. F. Johnson.)

52. How much does that account show over the period covered by it, that Alaska advanced in cash to R. Pedrante?      A. \$1510.

Q. How much did R. Pedrante pay in cash back to Alaska?      A. \$1834.61.

Q. Take the Medford Bargain House, Petitioner's 53 for identification. What cash advances are shown by the Alaska Junk Company to that account?      A. \$8000.

Q. Does it show any payments back to Alaska in cash?      A. Yes.

Q. How much?      A. \$11,182.36.

Q. Let us take the Steel Tank and Pipe Company, special [583] account. How much cash advance—that is Petitioner's 54—how much cash was advance to this company as shown by that account by Alaska Junk to the Steel Tank and Pipe Company?      A. \$1000.

Q. Does it show any payments back?

A. May I see the ledger card?

Q. Yes. (Hands document to witness.)

A. None in cash.

Q. Take Exhibit 55 for identification. That is the account of the Alaska Junk Company with Plumbing and Heating Sales Company. What does the account show as cash advances from Alaska to to the Plumbing and Heating Sales Company?

A. \$1050.

Q. Does it show any cash payments from

(Testimony of J. F. Johnson.)

Plumbing and Heating Sales Company to Alaska?

A. \$35,294.82.

Q. Are all the debits and credits I have mentioned in cash?

A. Cash debits and cash collections.

Q. We are not talking about any merchandise in these figures? A. That's right.

Mr. Jones: You may cross-examine.

Mr. Marcussen: If the Court please, counsel has just offered testimony concerning cash totals of all these [584] accounts which were marked for identification yesterday. Now, there were two or three of these concerning which he did not ask for testimony.

Mr. Jones: Two.

Mr. Marcussen: I don't know. It was either two or three. Counsel says it is two. With respect to those, the Respondent objects to those——

The Court: There was one that I remember which was not permitted because it was too remote. That will, of course, be excluded.

Mr. Marcussen: I will ask that they be stricken from the record.

The Court: The testimony will be stricken.

Mr. Marcussen: I am reluctant to have it in evidence at all.

The Court: My purpose in having the testimony was to cut the record short, and still have the pertinent facts.

Mr. Marcussen: May we discuss this off the record a moment?



(Testimony of J. F. Johnson.)

The Court: Yes.

(Discussion off the record.)

Mr. Marcussen: The witness testified from summaries that he prepared; and may it also be understood that we may have a copy of the summary, and I would like to offer these in evidence. [585]

Mr. Jones: These are working papers; they have nothing to do with it. You can offer those in evidence if you want to.

The Court: What is that that you are offering?

Mr. Jones: Those and the working sheets, and the adding machine tape.

Mr. Marcussen: I would like to offer them in evidence.

The Court: That would be what?

Mr. Marcussen: Respondent's DD, this yellow sheet, and EE for the adding machine tape for the sole purpose of enabling the Respondent to check the accuracy of these statements.

The Court: Very well.

(The documents referred to were marked and received in evidence as Respondent's Exhibits DD, and EE, respectively.)

The Court: Is there anything further?

Mr. Jones: That is all.

The Court: You may stand aside.

(Witness excused.)

The Court: Call your next witness.

Mr. Jones: That is the last witness for the Petitioner.

The Court: Does the Petitioner have any further testimony? [586]

Mr. Jones: That concludes our case. But I would like to say at this point that Mr. MacNaughton appeared as a witness out of order for the Respondent.

The Court: I think that is shown.

Mr. Marcussen: Yes, I think so.

The Court: Is Respondent ready to proceed?

Mr. Marcussen: Yes.

The Court: Very well, call your first witness.

Whereupon,

#### ARNOLD W. GROTH

recalled as a witness by and on behalf of the Respondent, having been previously sworn, was further examined and testified as follows:

#### Direct Examination

By Mr. Marcussen:

Q. Mr. Groth, do you remember the question that I asked you a little while ago when you were on the stand?

A. No, I don't recall it definitely.

Q. Would you like to have it read back to you?

A. Yes.

Mr. Marcussen: Do you think you will be able to find it in your notes, Mr. Reporter? If so, I would like to have it read back.

(Testimony of Arnold W. Groth.)

(Whereupon the question referred to was read aloud by the reporter as follows: "Can you state whether an application was made for a loan in the amount of \$400,000 by Oregon Steel in connection with an RFC loan?")

Q. (By Mr. Marcussen): Can you answer that?

A. I have a hazy recollection of that conversation which happened over six years ago.

The Court: Speak louder.

The Witness: As I say, I have a hazy recollection of that conversation. It happened over six years ago. But the file indicated that I did discuss that matter with the Legal Department.

The Court: Legal Department of the Bank?

The Witness: Of our Bank, because that is followed up by letters by our Mr. Zollinger to the RFC and to Mr. Morris Schnitzer. I might say that the application did not come before the Loan Committee evidently because it didn't have sufficient merit to bring it before the Loan Committee.

Q. (By Mr. Marcussen): Now, have you referred to this memorandum, Mr. Groth?

A. Yes.

Q. Do you recall what representations were made by Morris Schnitzer and Sam Schnitzer with reference to the application for a loan?

A. They gave certain information which was retained in the file.

(Testimony of Arnold W. Groth.)

Q. Can you tell us what it was? [588]

A. Whatever I wrote up, that would be it. I have read it. The note is that they needed a \$400,000 bank loan, and the statement was made that they were putting in certain money themselves and had made application to the RFC.

Q. Can you go ahead and state any more about it than you already have?

A. I think that is about all.

Q. Is that all you can remember?

A. Yes.

Q. Was this memorandum of April 15, 1942, in the bank files?           A. Yes.

Q. Was that prepared by you?           A. Yes.

Q. On the basis of that conference, with the Schnitzers, Morris and Sam, you made this memorandum?

A. That is our policy; any important conversation we write up as soon thereafter as possible.

Q. So far as you can recall at the time, this memorandum is what was dictated by you?

A. Yes.

Q. And was it your correct recollection of that conference with them?

A. Yes; I would write it up as nearly correct as possible. [589]

Mr. Marcussen: If your Honor please, the memorandum goes into considerable detail, and the witness says he does not recall it, that is, does not recall at all. I would like to offer it in evidence be-

(Testimony of Arnold W. Groth.)

cause he says it was correct at the time it was written up.

Mr. Jones: We object to it. We have no objection to his refreshing his memory from it.

The Court: Let him see if he can refresh his memory?

Mr. Marcussen: He has just gone over the memorandum at great length, and states that he is unable to refresh his recollection any further.

The Court: You cannot impeach your own witness.

Mr. Marcussen: I am not impeaching my witness, but I'm certain in a situation of this kind, if the document does not refresh his recollection, the document is permissible to provide a foundation,—I mean, is permissible provided a foundation is made to show that it was entered into at the time, and it was written down at the time in the due course of business, and that it was made by the witness who was there at the time.

The Court: Do you remember the fact that you made the document?

The Witness: I remember that, sir.

The Court: Do you know whether the document now [590] contains exactly what was said at the time by the parties?

The Witness: It contains exactly, as nearly as possible as I was able to put it on paper.

The Court: How soon after it was said was it put on paper?



(Testimony of Arnold W. Groth.)

The Witness: I cannot say; it all depends on the time we had in the bank. It is our policy to take care of the bank customers, and memorandums such as that are written up at the first opportunity that we have to do so.

The Court: When would that ordinarily be?

The Witness: I would say within 24 hours of the conversation.

The Court: I will overrule the objection.

Mr. Jones: May I save an exception?

The Court: You may have an exception, yes.

Mr. Marcussen: I offer that as Respondent's Exhibit next in order.

The Clerk: Respondent's FF.

The Court: It will be received as Respondent's FF.

(The document referred to was marked and received in evidence as Respondent's Exhibit FF.)

Mr. Marcussen: And with respect to this or any other document which may be referred to from the file, I would like to have the privilege of submitting a photostatic copy.

The Court: That permission has been granted many [591] times, for the past, present and future. Are there any further questions of this witness?

Mr. Marcussen: Yes; I have another document here.

Q. (By Mr. Marcussen): Who consulted you about loans from time to time in the early part

(Testimony of Arnold W. Groth.)

of 1941 or 1942 with respect to a loan either directly to Oregon Steel or to its stockholders for the purpose of advancement to Oregon Steel?

A. It might be either Morris Schnitzer, Samuel Schnitzer or Harry Wolf.

Q. Did you have conferences with them from time to time? A. Oh, yes.

Q. Do you recall, on the basis of the conferences, what the representations were that were made to you concerning the proposed authorization of capital stock?

The Court: By Oregon Steel, you mean?

Mr. Marcussen: Yes.

The Court: The authorized capital of Oregon Steel?

Mr. Marcussen: Authorized capital or issued capital of Oregon Steel.

A. That was discussed from time to time.

Q. (By Mr. Marcussen): Do you recall what statements were made to you?

A. What dates? [592]

Q. At any time during this period in 1941 and 1942?

A. Yes, there were various conferences. The situation moved along; it started out with a certain amount of capital which was added to from time to time. The credit reports which we wrote up for our own records which had the approval of our Loan Committee would indicate such conversations as we had in connection with the loan application.

(Testimony of Arnold W. Groth.)

Q. Do you remember any specific figure?

A. No, I don't remember.

Q. Would you get the letter that you wrote under date of June 25, 1942, to Mr. Knauff, credit manager of the Columbia Steel Company of Portland?

A. Yes, I have that June 25, 1942, letter.

Q. Did you write that letter?

A. Yes.

Q. Did you sign it?

A. I signed that letter.

The Court: What is the date of it?

The Witness: June 25, 1942.

Q. (By Mr. Marcussen): Does that letter refresh your recollection as to what the authorized capital of Oregon Steel was to be?

Mr. Jones: Just a minute.

Mr. Marcussen: I am asking him whether it refreshes his recollection or not. [593]

Q. (By Mr. Marcussen): Does it?

A. It does not.

Q. It does not? A. No, sir.

Q. This letter was prepared by you?

A. That is correct. There is no definite amount stated in the letter,—well, the letter says this,—

Mr. Jones: Just a minute.

Q. (By Mr. Marcussen): Does that refresh your recollection?

A. Yes, to that extent. In other words, I cannot give you any exact amount.

Q. Does the letter contain a statement of an

(Testimony of Arnold W. Groth.)

amount that you understood to be the authorized capital?      A. Yes.

Q. Now, please don't answer this if counsel has an objection. I ask you to state what the amount was?

Mr. Jones: Before he answers, I would like to ask where he got the information.

Mr. Marcussen: I have already established that fact in the evidence, on the basis of conferences he had with Alaska Junk and Oregon Steel.

The Court: Is that information, again, from officers of Alaska Junk and Oregon Steel?

The Witness: I would say, as near as I can remember, yes. [594]

Mr. Jones: May I ask a question or two first?

Mr. Jones: Do you know who gave you the information, Mr. Groth, which indicates the figure in the first paragraph?

The Witness: I could not tell you which party gave it to me.

Q. (By Mr. Marcussen): Do you know whether it was Sam or Harry or Morris?

A. It might have been any one of the three.

Mr. Jones: Could it have been anyone else?

The Witness: That is possible.

Mr. Jones: Until the witness more clearly indicates the source of the information, we object to it as incompetent, irrelevant and immaterial, and purely hearsay, and in no way connected with or identified with any party to these proceedings.

(Testimony of Arnold W. Groth.)

Mr. Marcussen: The evidence shows that this witness had numerous conferences with the stockholders of Oregon Steel, who were the principals in the Alaska Junk, concerning an application for a loan, and concerning the intentions of this company, and he identified them as the source of his information; and he said it might have come from any one of the three. The mere fact that it might have come from any other place does not disqualify the evidence.

The Court: What is your best judgment as to the source from which you obtained that? [595]

The Witness: It might have come from Mr. Harry Wolf, Mr. Sam Schnitzer, or Mr. Morris Schnitzer, or the RFC.

The Court: What is your best judgment as to the source from which it came; would you say it came from one of the three?

The Witness: I could not say definitely.

The Court: What is your best knowledge and belief?

The Witness: My best knowledge and belief is that it did come from one of the three.

Mr. Jones: May I have an exception?

The Court: Yes.

Q. (By Mr. Marcussen): Will you state what the authorized capital of the company was to be, according to your recollection?

A. It does, in part: "We understand it has an authorized capital of \$1,000,000; however, we are



(Testimony of Arnold W. Groth.)

not advised as to the amount actually paid in." The "it" refers to Oregon Steel.

Q. How did you sign the letter?

A. As Vice President.

Q. And that was on the Bank's stationery,—the original? A. Yes.

Q. Well, do you recall in the course of your conversation with these individuals, any specifically stated amount? Do you recall what the amount of the paid-in capital would be? [596]

A. At what date?

Q. At any time, Mr. Groth.

A. I don't remember.

Q. I would like to have you refer to the letter which you wrote on March 3, 1943, to Clipper Manufacturing Company.

The Court: Does the witness identify that letter as one which he has written?

Mr. Marcussen: No. I just asked him to refer to the letter.

The Court: He has the letter in front of him?

Mr. Marcussen: He has the file.

Q. (By Mr. Marcussen): Have you found that letter? A. Yes.

Q. Will you read it, please?

A. What is the question?

Q. I just asked you to refer to the letter; does that letter refresh your recollection?

A. To some extent.

(Testimony of Arnold W. Groth.)

Q. And could you testify as to what it would be without reference to the letter?

A. No, I would not remember unless I read the letter.

Mr. Marcussen: If your Honor please, I would like to read into the record the pertinent portion of that letter.

Mr. Jones: I object to his reading it into the record. The witness could not recall it.

The Court: Did he say his memory was refreshed?

Mr. Marcussen: He said he could not testify without reading the letter.

The Court: Based on refreshing your memory from the letter, are you able to say, from the best knowledge and belief, what the facts are in that letter?

Q. (By Mr. Marcussen): Can you do that without reading the letter?

A. What is the question?

The Court: Does that letter refresh your recollection so that you can testify?

The Witness: What the paid-in capital was to be?

Q. (By Mr. Marcussen): What the paid-in capital was to be by the stockholders? A. No.

Q. You cannot do it without referring to the letter?

A. I would have to refer to the letter.

The Court: You cannot tell from the reading

(Testimony of Arnold W. Groth.)

of the letter whether your memory is refreshed?  
In other words, your memory is not so refreshed?

The Witness: That is correct.

The Court: You could not testify to the fact without reading the letter? [598]

The Witness: I would have to read the letter.

The Court: You have now read the letter. Has your memory been refreshed so that you can testify?

The Witness: I would say not.

The Court: That letter, can you identify that as having been written by you?

The Witness: Yes.

The Court: And do you know that the facts contained therein were true as you understood them at the time?

The Witness: Yes.

The Court: Where did you get the letter that you gave to counsel?

The Witness: From the files.

The Court: Where did you get the information that was put down in the letter?

The Witness: It might have come from a number of sources; it might have been as a result of a conference with Mr. Harry J. Wolf, Sam Schnitzer, or Morris Schnitzer.

The Court: To the best of your judgment, where did you get it?

The Witness: I think from one of the three.

(Testimony of Arnold W. Groth.)

Q. (By Mr. Marcussen): Was that written on the bank's stationery? A. Yes.

Q. Did you sign it? [599] A. Yes.

Mr. Marcussen: If your Honor please, may I read it into the record?

Mr. Jones: May I have an objection to that as incompetent, irrelevant and immaterial.

The Court: The Petitioner makes an objection, and I will overrule the objection, and an exception will be noted.

Mr. Marcussen: I will read the first paragraph: "In reply to yours of the 27th *untimo* regarding the Oregon Electric Steel Rolling Mills, have to advise that this company was formed about a year ago to engage in the manufacture of steel in this city. We are advised that the stockholders are paying about \$500,000 and that the RFC has agreed to advance them a sum substantially in excess of the paid-in capital on the basis of a first mortgage on land, buildings, and equipment, etc."

Q. (By Mr. Marcussen): Mr. Groth, in the course of your conversations with Harry, Sam Schnitzer and Morris Schnitzer, do you recall any statements made by them to you concerning the total amount it would take to build the plant, that is, the cost of the mill itself?

A. I don't remember.

Q. Do you have any recollection of what the total amount of the capital surplus was going to be? A. I don't remember. [600]

(Testimony of Arnold W. Groth.)

Q. Nor the capital stock?

A. No. I might amplify that by saying that in making loans to the company, we are not concerned so much by the amount of capital stock as we are about the current financial position and its ability to repay the loan.

Q. I will ask you about that letter, Mr. Groth——

The Court: I didn't hear you.

Mr. Marcussen: Pardon me.

Q. (By Mr. Marcussen): I will refer to a copy of a memorandum which you prepared under date of December 12, 1941, and I will ask you to state what that document is that is in the file? (Hands document to witness.)

A. That is a memorandum that I prepared as of December 12, 1941, giving information at a meeting of the Advisory Council of the Reconstruction Finance Corporation at Portland. Incidentally, I might say——

The Court: You mean concerning this Oregon Steel?

The Witness: Concerning the Oregon Steel Mill. I might say that I am a member of the Advisory Council of the RFC, and that accounts for this memorandum being placed in our credit files.

Q. (By Mr. Marcusen): First, let me ask you this: you received this information that appears on that memorandum from the RFC? [601]

A. At a meeting at the RFC.



(Testimony of Arnold W. Groth.)

Q. And I think you stated to the court that you are a member of the Advisory Board?

A. Advisory Council.

Q. Of the RFC? A. Portland Agency.

Q. It was a part of your duties to ascertain concerning principals to whom the bank had been loaning money? A. Oregon Steel in this case.

Q. How about the principals of the Oregon Steel—the stockholders of Oregon Steel.

A. I don't understand your question.

This is a memorandum in connection with a loan application made by Oregon Steel at the RFC.

Q. And you placed that in your files for whatever benefit it might be with relation to the credit line of the Oregon Steel and its stockholders?

A. Yes.

Q. Does that refresh your recollection as to what the total cost of the mill was going to be, and as to what the amount of capital stock was going to be, and the amount that the surplus was going to be, and the total amount that was to be provided by stockholders?

A. If I read the paragraph it would give the facts as I understood them as of December 12, 1941. I cannot memorize [602] these things.

The Court: Do you have an independent recollection that those figures are correct?

The Witness: I would say that those figures are correct.

(Testimony of Arnold W. Groth.)

The Court: From what source did you get the information?

The Witness: At a meeting of the RFC.

The Court: Did the Petitioners have anything to do with the meeting which gave the information to the RFC?

The Witness: I assume the officers of the Oregon Steel; they made the application.

The Court: It was in the application?

The Witness: Yes, sir; information — supplementary information.

The Court: Oregon Steel had made an application to the RFC for a loan?

The Witness: That is right.

The Court: And this information is contained therein?

The Witness: That is correct.

Mr. Jones: May I examine that before you go any further, please?

The Court: Is there any objection?

Mr. Jones: Yes; we feel it is cumulative and that it is incompetent, irrelevant and immaterial and hearsay. [603]

The Court: I will overrule the objection.

Mr. Jones: May I save an exception?

The Court: Yes.

Mr. Marcussen: If Your Honor please, I would like to read from the memorandum the second paragraph, as follows: "The preliminary figures showed that it would take \$952,000 to complete the

(Testimony of Arnold W. Groth.)

mill, and that \$100,000 working capital would be required. The application was for an RFC loan of \$600,000, to be repaid over a ten year period. Thus the amount that the stockholders would have to provide would be \$452,000. The application provided for \$250,000 of capital stock and surplus of \$202,000. Morris Schnitzer was shown to be the owner of 50 per cent of the capital stock, Sam Schnitzer 25 per cent, and Harry Wolf 25 per cent. Thus the amount that they would have to provide on the basis of the preliminary figures would be a cash outlay of \$452,000. It provided that Sam Schnitzer and Harry Wolf and their wives would personally guarantee up to \$200,000 of the \$600,000 loan; this guarantee was to be continued regardless of what reduction is made on the \$600,000."

Mr. Jones: The stock ownership memoranda must be stricken because it conflicts with the stipulation.

The Court: If it conflicts with the stipulation, of course it must be stricken.

Mr. Marcussen: What part of the stipulation. If you will please show me what paragraph you are referring to?

Mr. Jones: Very well. May we go off the record?

The Court: Off the record.

(Discussion off the record.)

Mr. Marcussen: The only paragraphs of the stipulation to which he refers as being inconsistent

(Testimony of Arnold W. Groth.)

would be the paragraphs 11, 12, 13, 14, 15, and, I suppose 17.

The Court: What do they show?

Mr. Marcussen: All they do is recite what stock was actually issued; they have nothing to do with the proposals that were made for the amount of capital which was to be invested in this enterprise by the stockholders. If that is true, then practically two thirds of the evidence that has been introduced should also be stricken, if that is the proper interpretation of the stipulation.

The Court: Will you ask him the portion which he contends should be stricken?

Mr. Jones: This shows that Morris Schnitzer was shown to be the owner of 50 per cent of the capital stock.

The Witness: That's right.

Mr. Jones: And then it says that Sam Schnitzer was to have 25 per cent and Harry Wolf 25 per cent, while the two of them together only had 25 per cent.

Mr. Marcussen: That is not a part of the stipulation, [605] counsel. I refer Your Honor to paragraph 14 of the stipulation, which shows that as of March 11, 1943——

Mr. Jones: That is 1941.

The Witness: Yes; December 12, 1941.

The Court: The stipulation on page six, the middle of the page, paragraph 14.

Mr. Marcussen: Yes. It shows Morris Schnitzer

(Testimony of Arnold W. Groth.)

was the owner of 625 shares of stock and Alaska Junk in toto was the owner of, well, roughly, another half; so the statement contained in here is not in conflict with it, and merely purports to be a statement—well if Your Honor please——

The Court: I think here is what the court will do in this matter.

Mr. Marcussen: I will stipulate the withdrawal of that portion.

The Court: The Court will admit it, subject to the Court's further consideration, if he finds the provisions of the stipulation are in conflict, it will be disregarded.

Mr. Jones: Counsel has already stipulated it is in conflict.

The Court: All right. If it is in conflict, it will be stricken.

Mr. Marcussen: I am willing that this following part may be stricken: "Morris Schnitzer was shown to be the owner of 50 per cent of the capital stock, Sam Schnitzer 25 per cent [606] and Harry Wolf 25 per cent."

The Court: That part will be stricken.

Mr. Jones: Yes.

Mr. Marcussen: My apologies to Court and counsel.

The Court: That portion will be deleted from the testimony. All right, proceed with the witness if you have any further questions. Perhaps this would be a good time to take a recess. We will take a five



(Testimony of Arnold W. Groth.)

minute recess at this time, after which I will ask counsel to be ready to proceed with the testimony.

(Whereupon a short recess was taken.)

Q. (By Mr. Marcussen): Mr. Groth, do you know whether or not the application of the Oregon Steel and its stockholders for a loan of \$400,000 was rejected by the bank?

Mr. Jones: If the Court please, he has already gone into that.

The Court: He testified to that.

Q. (By Mr. Marcussen): Well now, will you state, please, what was the reason the bank rejected that loan?

The Court: It just reached a preliminary stage; it didn't reach the Loan Committee, as I understand it.

The Witness: It did not reject it. It did not reach that stage. [607]

Q. (By Mr. Marcussen): Why was it circumvented from the Committee? Did you notify the parties there was no loan to be granted?

A. Oh, I don't remember; I presume I did. Someone did; either Mr. MacNaughton or myself.

Q. You handled the application, didn't you?

A. I really don't recall; it was more of an informal matter, and I really didn't call it an application. It was a discussion of the possibility of an application of a \$400,000 loan.

(Testimony of Arnold W. Groth.)

Q. What was the reason the Loan Committee was not asked to consider it?

A. Well, in first place, there was inadequate capital; second, inexperience in that particular line of business; no final arrangement for a long-term loan with the RFC. It was too weak to even present to the Committee.

Mr. Marcussen: That is all.

### Cross-Examination

By Mr. Jones:

Q. Mr. Groth, when some of these representations that you have referred to were made by certain people, you think, as I gather it, that those representations were made by the three people that you mentioned. However, you could have gathered that information almost anywhere in conversations, could you not? [608]

A. If you will take out the word "anywhere," I would say it could be gathered from people and other concerns that I had conversations with relative to Oregon Steel.

Q. Well, it might have been someone other than Sam Schnitzer, Harry Wolf or Morris Schnitzer?

A. Yes; it might have been information that I gathered at the Reconstruction Finance Corporation meetings.

Q. The last exhibit that was referred to and was read into the record and which bore a date, I believe, of 1941, that was a report that you made from the Loan Committee conference at the RFC?

(Testimony of Arnold W. Groth.)

A. That is correct.

Q. May I see it?

A. Yes; it is right here. (Hands document to counsel.)

Q. Do you know that this corporation was organized on June 4, 1941?

A. I don't remember the exact date.

Q. Well, it was organized and commenced its corporate life on June 4, 1941. There is no question about that?

A. I don't know.

Q. Did you know that at the time the letters were written?

A. I would say yes.

Q. Now, when you are attempting to determine the capital structure of a corporation, is it the custom of the [609] bank to go up to the Courthouse to see what is authorized?

A. Not necessarily. In the case of responsible people, such as the Schnitzers and Wolfs with whom we have had business dealings over a period of years, and who have always worked in close co-operation with us and in entire honesty with the bank, we would take their word for it, whatever they would say.

Q. Did you know that the authorized capital stock as of June 4, 1941, was set at \$250,000?

A. I did not know. In any event, I would not be interested in the authorized capital stock. I would be, rather, interested in how much cash was laid on the barrelhead; that is what would most interest us.

(Testimony of Arnold W. Groth.)

Q. There are statements in your letters of 1942 and 1943, speaking in one place of \$500,000 capital and an investment of something like \$1,000,000 in the other.

A. \$1,000,000 authorized capital, as I remember the letter.

Q. Well, did you realize or did you know at the time whether the capital structure was increased at any time from its inception, from \$250,000?

A. I am not familiar with that.

Q. Do you know that only \$187,800 worth of stock was ever issued?

A. I don't know that.

Q. Do you know that that was the only capital stock that [610] has ever been issued up to date in the hands of the new owners?

A. I don't know that. Capital structure doesn't mean anything in a bank. What we are interested in is net worth; that is what we are looking at; that is what interests us.

Q. What I am trying to point out is that with respect to the information that you had in the letters, and from whatever source it was gathered, it was erroneously recorded?

A. That's possible. We attempt to answer letters of inquiry to the best of our ability; we try to get all the information as accurately as we can. It is entirely possible that all the information that is contained in that file is not accurate; but it is



(Testimony of Arnold W. Groth.)

the best information we are able to get, perhaps, quickly and under the circumstances.

Q. Of course. In dealing with Mr. Sam Schnitzer and Mr. Harry Wolf, didn't you find out in dealing with them that their exact use of business terms was not accurate? A. I think that is true.

Q. And if they had actually extended credit and it represented some money to them, they might refer to it at one time as an investment, and at another time as an advance? Is that correct?

Mr. Marcussen: I will object to that. There is nothing in here that refers to advances or investments.

The Court: I will overrule the objection.

A. I think that is probably true. [611]

Q. (By Mr. Jones): And didn't you find that they would very likely put the wrong accountant's term or the wrong legal term on what the situation was?

A. In case of Mr. Wolf and Mr. Schnitzer, that is entirely possible.

Q. And a good deal of this information may have come to you through Mr. Sam Schnitzer or Mr. Harry Wolf?

A. Or Mr. Morris Schnitzer.

Q. Let us confine it to the two. Couldn't a good deal of it have come Mr. Sam Schnitzer and Mr. Harry Wolf? A. Yes, indeed.

Q. And the amounts that they had in mind as obligations could very well have been accurate, as



(Testimony of Arnold W. Groth.)

you stated them, but their nomenclature might have been erroneous?

A. They might have, in fact, been referring to advances by the stockholders or investment in capital stock. It might mean that they had an investment of so much money.

Q. And it might be from a lawyer's or an accountant's standpoint purely an accounts receivable?

A. That is possible, yes.

Mr. Jones: Did you intend to call Mr. Zollinger, on this, Mr. Marcussen?

Mr. Marcussen: No sir.

Q. (By Mr. Jones): Who was this Mr. Zollinger who wrote a letter [612] which expressed the reason why the \$400,000 was not granted?

A. Mr. Zollinger wrote the letter dated April 12, or whatever date it was.

Mr. Marcussen: April 22, 1942, Mr. Groth, to Morris Schnitzer.

Q. (By Mr. Jones): Now, isn't it true that one of the reasons or perhaps the main reason for you not making the \$400,000 loan was because of the conditions of the principal loan to the RFC; that is, the conditions of the principal loan to the RFC were not satisfactory to you?

A. That was one condition.

Q. That was the condition that primarily Mr. Zollinger had in mind; he didn't like the way it was set up?

A. Plus the fact it was inadequate capital; plus

(Testimony of Arnold W. Groth.)

the fact that they were inexperienced in the manufacture of steel.

Q. Now, as to some of the conversations that you are referring to in some of these memoranda that you referred to, a good deal of it referred to conversation with respect to plans and projects in mind?

A. Yes.

Q. And that some of it was not crystallized, and was just in the planning and expectation stage?

A. Correct.

Q. You do not represent, or purport to represent that [613] the memoranda to which you have referred reflects——

Mr. Marcussen: May we have it identified. I don't know what you are talking about.

Mr. Jones: I am talking about the documents that you put in. One was marked FF and one was marked following that; and then there were others which were used to refresh his memory with respect to the facts that we are talking about.

Q. (By Mr. Jones): A good deal of the material was merely plans and expectations that they talked about. And now my question is, you don't know exactly how much of that was actually put into practice or how it worked out?

A. I would have no way of knowing.

Mr. Jones: That is all.

Mr. Marcussen: Just one or two questions on redirect.

(Testimony of Arnold W. Groth.)

Redirect Examination

By Mr. Marcussen:

Q. I will point out to you a carbon copy of a letter in the bank files, dated April 22, 1942, addressed to Mr. Morris Schnitzer and purporting to be a letter from Mr. C. E. Zollinger, assistant Vice President, and I will ask you to refer to that letter.

A. All right.

Q. I will ask you if that letter to Mr. Schnitzer is the letter in which an application for a loan is rejected and [614] the reasons given for rejection?

A. The so-called \$400,000 loan?

Q. Yes.           A. Yes.

Q. Do you know whether that was sent out in the regular course of mail?

A. I am not sure. I would say that if Mr. Morris Schnitzer was present, it would have been handed to him. He might have been present.

Q. It was either one of those two methods, either being handed to him personally or being sent through the mail?           A. That's right.

Mr. Marcussen: I will offer that.

Mr. Jones: For one thing, it is not proper cross-examination.

The Court: Did the witness write the letter.

The Witness: I did not.

Mr. Marcussen: He has identified it as a letter. I can call another witness who did write it.

The Court: Is there any doubt that Mr. Zollinger wrote the letter?

(Testimony of Arnold W. Groth.)

The Witness: In my opinion he wrote the letter.

Q. (By Mr. Marcussen): In the regular course of the bank's business? A. Yes. [615]

Q. Is there any doubt about it?

A. None at all.

Q. And in the regular course of the bank's business? A. Yes, in my opinion.

Q. If that letter had not been written or put into the hands of Mr. Schnitzer, would it have been in the files?

A. If it had not been delivered to Mr. Schnitzer, it would not have been in the files.

Mr. Jones: May I state my objection?

The Court: Surely.

Mr. Jones: On direct examination he referred to the reasons why the loan was not granted, and then I picked up this letter and asked him if the reason stated was that. I object to this going in as an exhibit on rebuttal examination.

Mr. Marcussen: I will withdraw the offer.

The Court: The offer is withdrawn.

Q. (By Mr. Marcussen): When you prepare these memoranda of these conferences, or when you prepared these specific ones with Mr. Sam Schnitzer and Harry Wolf and Morris Schnitzer, were you satisfied when you put the information down, that the information was correct at the time?

A. There would be no reason for putting down incorrect information; naturally, when I put it down, I thought it was the correct [616] informa-



(Testimony of Arnold W. Groth.)

tion, and I stated it as briefly as I could possibly state it in connection with the conversation.

Q. At the time you had these conferences, were you fully aware—I think you testified on cross-examination that you were quite aware at time of the inadequacy of their nomenclature and their terms and that sort of thing. A. Yes.

Q. Did you make any effort ascertain exactly what they meant? A. No.

Q. You did not?

A. No. In other words, they told me they had a half a million dollars paid in capital, and that is what I placed in the letter. I didn't try to determine whether it was capital advances or capital stock. We had confidence in the Schnitzer family and the Wolf family, based on many years of successful banking experience, and we took their word.

Q. Do you happen to know whether they used the exact terms that you used in the memorandum?

A. In all probability, the terms that they used were reflected in the memorandum.

Q. You were aware at the time the information was given to you of any lack of familiarity on their part, or their lack of familiarity with financial terms as you might use them? [617]

A. That is correct.

Q. Did it occur to you that the memorandum might be confusing, or were you interested in finding out what they did mean in making your decision in the bank.



(Testimony of Arnold W. Groth.)

A. When it came time to loan money, we didn't loan it on the memorandum. We would make a loan on secured collateral, or pledged collateral; and any data that we would have in there would be supplementary.

Mr. Marcussen: That's all.

Mr. Jones: That's all.

The Court: You may stand aside.

(Witness excused.)

Mr. Marcussen: I will call Mr. Zollinger.

Whereupon,

C. E. ZOLLINGER

called as a witness by and on behalf of the Respondent, having been first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Marcussen:

Q. Will you state your name?

A. C. E. Zollinger.

Q. What is your position in the bank, Mr. Zollinger?

A. Vice-President of the First National Bank of Portland.

Q. How long have you been vice-president of the bank? [618]

A. Three or four years, I should think.

Q. And what was your position in the month of April, 1942?

(Testimony of C. E. Zollinger.)

A. I was Assistant Vice-President at the time.

Q. In the course of your duties as Assistant Vice-President, did you have occasion to confer with Mr. Groth and other officers of the bank on the application of the Oregon Steel Electric Rolling Mills for a loan?

A. I could not make a complete answer to that question, Mr. Jones. I am sure that I had a conference with someone in the bank, probably Mr. Groth or Mr. MacNaughton; and I also talked, I think, with Mr. Morris Schnitzer and also with Mr. Harry Wolf and Sam Schnitzer.

Q. Do you recall whether it was your duty to either write a letter or hand it to Mr. Morris Schnitzer, containing your decision with respect to the application for a loan?

A. I wrote that letter.

Q. I hand you the bank's file and ask you if you can point out that letter? (Hands file to witness.)

A. Yes; that is a letter dated April 22, 1942, which I directed to Mr. Morris Schnitzer.

Q. And looking at the heading there, can you ascertain from the first page of the letter whether it was handed to him or whether it was mailed to him?

A. Yes, it was handed to him. As I remember, I had a [619] conference with him and he expected to call on me the following day, so I directed that it was to be delivered in that manner.

(Testimony of C. E. Zollinger.)

Q. Will you state for the record how many pages there are to this letter?

A. The letter as originally transcribed was two full pages, and a paragraph on the third page. The first page was revised after it had been written, and is marked here with some rather fine lead pencil markings, so that it now appears in three pages; on the first page and on the reverse of the first page of the original draft, and on the third page, which is marked sheet number two, but is actually the third page of writing.

Q. Which of those two first pages was actually dispatched?

A. The one that has no writing on the reverse. The letter, as dispatched, consisted of a first page, which appears in the file without any writing on the reverse, and the second page which appears on the reverse of the original draft of the first page and a third page which has no writing on the reverse page.

Q. Will you take the pencil and mark those pages, please, in red, and put a circle around your initials on the second and third pages of that letter as actually handed to Mr. Schnitzer?

A. I have marked each of the pages in red pencil, page [620] one, page two and page three.

Q. I call your attention to the pencil marks on the left margin of page one of the letter; that was not on the original, was it?

(Testimony of C. E. Zollinger.)

A. That was not on the original; I don't know when that mark was made.

Mr. Marcussen: I offer those pages in evidence as a Respondent Exhibit next in order, if the Court please.

Mr. Jones: May I take a look at it?

Mr. Marcussen: Certainly. (Hands document to counsel.)

Mr. Jones: We object to it as incompetent, irrelevant and immaterial; it doesn't go to prove any issue in the case; it is purely hearsay, and it concerns reasons for rejecting a loan that they never made, and it involves nothing that went into the capital structure of the company.

The Court: May I see it?

Mr. Marcussen: Yes, Your Honor; it is just simply one of the chain of events in the attempt of Oregon Steel to finance itself.

The Court: I will overrule the objection.

Mr. Jones: Save an exception.

The Court: Yes. What number will that be?

The Clerk: GG.

The Court: It will be admitted in evidence and marked as Respondent's GG.

(The document referred to was marked and received in evidence as Respondent's Exhibit GG.)

Mr. Marcussen: I have no further questions of this witness.

(Testimony of C. E. Zollinger.)

The Court: Is there any cross-examination.

Mr. Jones: No cross-examination.

The Court: You may stand aside.

(Witness excused.)

The Court: Call your next witness.

Mr. Marcussen: I will call Mr. Cruickshank.

Whereupon,

**JAMES H. CRUICKSHANK**

called as a witness by and on behalf of the Respondent, having been first duly sworn, was examined and testified as follows:

**Direct Examination**

By Mr. Marcussen:

Q. Will you state your name?

A. James H. Cruickshank.

Q. How do you spell it?

A. Cruickshank. (Spelling.)

Q. What is your business?

A. Assistant manager, Portland Loan Agency of the Reconstruction Finance Corporation. [622]

Q. How long have you occupied that position?

A. Since December 1941.

Q. How long have you been with the RFC?

A. Since March 2, 1932.

Q. As Assistant Manager, will you please describe generally what your functions and duties are?

A. Well, I assist in the overall management of



(Testimony of James H. Cruickshank.)

the agency; and in the absence of the manager, I am the acting manager.

Q. Do you participate to some extent in the passing on applications for loans made at the corporation?

A. I am a member of the Review Committee, the loan committee.

Q. Prior to 1941, what were your duties?

A. Well, immediately prior to that I was head of the Loan Application Division.

Q. How long were you acting in that capacity?

A. Three or four years, I believe.

Q. What were your duties in that capacity?

A. Well, I had supervision over the examiners who handled the loan applications; I reviewed their work and audited the reports, and had general supervision.

Q. During the three or four years you were acting in that capacity, just what capacity was that?

A. I was an examiner handling loan applications.

Q. As an examiner, will you state what your duties were in handling the loan applications?

A. That was prior to that. I have been engaged, you might say, in that same line of work ever since I have been there, only in a lesser capacity.

Q. As an examiner, will you state what your duties were in handling loan applications?

A. When a loan application comes in, you make the usual credit inquiries as to the standing of the company and the management; you inspect their

(Testimony of James H. Cruickshank.)

properties and analyze the financial and operating statements; you write a report of your findings and make a recommendation to the Review Committee and the management as to whether or not the loan should be made.

Q. In the course of the performance of those duties and the other duties that you may have performed at the RFC, have you acquired a thorough knowledge of the financial statements, and their analyses and that sort of thing?

A. I think so, yes.

Q. And are you familiar with the Oregon Electric Steel Rolling Mills, that we will hereafter refer to as "Oregon Steel"?

A. In a general way, yes.

Q. And from time to time have you had something to do with the passage of that application through the office? [624]

A. In a general way, yes.

Q. And from time to time have you had something to do with the passage of that application through the office? A. Yes.

Q. And do you have a general familiarity with it? A. Yes, I do.

Q. Now, do you recall what the total assets of the Oregon Steel were when it was finished?

A. No, I do not.

Q. I hand you Exhibit 19, which is a balance sheet of the corporation as of October 31, 1943. I call your attention to the fact that the total assets

(Testimony of James H. Cruickshank.)

are approximately \$1,869,000. With an industrial corporation of that size, can you state, from the point of view of sound financing what the ratio of the capital and net worth would be to total liabilities?

Mr. Jones: If Your Honor please, we object to that as calling for a conclusion of the witness on a theoretical subject, in a theoretical field.

The Court: I will overrule the objection.

Mr. Jones: May I save an exception?

The Court: An exception will be noted.

A. Well, in a general way, we feel that the net worth should exceed the total liabilities for sound financing. [625]

Q. (By Mr. Marcussen): And in the case of a new corporation having, just for example, \$2,000,000 worth of assets, which would mean that the capital and the net worth would be half of that figure, would it not?

A. I don't think I stated it. I was about to state it. The net worth should exceed the total liabilities for sound financing by a ratio of about two to one.

Q. In understood you to say that.

A. That is what I was about to say.

Q. Having that in mind, in the case of a new corporation with \$2,000,000 worth of assets, that would mean that the capital and the total net worth would be half of that figure, would it not?

A. That is right.

Q. On the basis of that testimony?

(Testimony of James H. Cruickshank.)

A. Yes.

Q. And the other half of that figure would be represented by liabilities?

Mr. Jones: I object to that as leading the witness.

The Court: I don't think a leading question is proper at this stage.

Q. (By Mr. Marcussen): I will ask you to state then, in the case of a \$2,000,000 *dollar* corporation, from the point of view of sound [626] financing——

Mr. Jones: That accomplishes the same thing. He has already led him up to it, and now he wants to say it over again.

The Court: The witness is intelligent. I don't think he is influenced in any way. Go ahead.

Q. (By Mr. Marcussen): In the case of a corporation having *of* assets of \$2,000,000, what would you say was the amount of net worth, including capital and surplus——

Mr. Jones: It is leading.

The Court: Go ahead.

Mr. Marcussen: I will start again.

Q. (By Mr. Marcussen): In the case of a corporation having assets of \$2,000,000, what would you say the amount of net worth, including capital stock and surplus should be?

A. Not less than \$1,000,000 ordinarily.

Mr. Jones: Just a moment. Under the rules of law, I move that the answer be stricken, because it is the intention of the parties, what they wanted



(Testimony of James H. Cruickshank.)

to invest, whether they were investing or extending credit; that would be the governing thing, their intention, and not some classical rule of economics.

The Court: You may cross-examine when your time comes.

Mr. Marcussen: It is the Government's contention [627] now, if the Court please.

The Court: I don't want to hear the discussion. The Court has ruled.

Mr. Marcussen: Very well.

Mr. Jones: May I note an exception to Your Honor's ruling?

The Court: Yes; an exception will be noted.

Q. (By Mr. Marcussen): Do you know how much capital stock was paid for by the stockholders of Oregon Steel?

The Court: Is that stipulated?

Mr. Marcussen: It is stipulated that it was about \$187,000.

The Witness: Yes.

Q. (By Mr. Marcussen): And the balance sheet, Exhibit 19, I think reflects that, does it not?

A. Yes.

Q. I call your attention to the fact that the RFC granted a loan to this corporation which, as of the date of this balance sheet was stated in the amount of \$678,843.70. Can you tell me what steps were taken by the bank to protect that loan in view of the small amount of capital actually contributed by the stockholders?



(Testimony of James H. Cruickshank.)

Mr. Jones: Well now, in the first [628] place——

The Court: He was not with the bank.

Mr. Marcussen: I mean, with the corporation, the RFC.

Mr. Jones: That assumes a fact that has not been proven.

The Court: Yes; he is your witness. Ask him the question, do not assume a fact not proven.

Mr. Marcussen: I would like to strike the question insofar as the word “small” appears in there and characterizes the amount of the contribution. Otherwise, I will let the question stand.

The Court: Your question assumes certain things had been done, about which the witness has not been asked.

Mr. Marcussen: There are a lot of things in evidence here which have been assumed.

The Court: Possibly so, but he is testifying as your witness.

Mr. Marcussen: If Your Honor please, I would like to ask him about the facts in this case.

The Court: Ask the witness. To that question, the objection is sustained.

Q. (By Mr. Marcussen): What steps did the RFC take to protect the first mortgage loan?

Mr. Jones: I will object to that. [629]

Q. (By Mr. Marcussen): I hand you Respondent's Exhibits C and D, and ask you to state what they are.

Mr. Jones: Those exhibits speak for themselves.

(Testimony of James H. Cruickshank.)

The Court: You don't have to ask the witness what they are.

Mr. Marcussen: Do you understand what they are?

The Witness: Yes.

The Court: Tell him what they are if he doesn't know it, and go on with the questioning.

Q. (By Mr. Marcussen): What was the purpose? I pointed out to you that these are standby agreements, which run in favor of the corporation.

The Court: What corporation do you have reference to?

Mr. Marcussen: In favor of the RFC.

The Court: All right. Call it the RFC.

Mr. Marcussen: And that it included the Oregon Electric Steel Rolling Mills as an operator, and certain individuals as standby creditors.

Q. (By Mr. Marcussen): Will you explain what standby creditors?

A. These people were advancing money——

Q. In the first place, what is meant by standby creditors? [630]

A. Well, if a concern owes money to certain individuals, they agree to stand aside or to wait, or to waive any action on their part to assert their claims as creditors, until certain other conditions have been met. In the case of the RFC, they would stand by in deference to the RFC loan.

Q. Until when?

A. Until the RFC's debt is extinguished, or until

(Testimony of James H. Cruickshank.)

they get the consent of the RFC to make payment.

Q. Can you state what the comparative position of the RFC is on its loan with respect to the prospect of payment, in general, or the point of view of the RFC as between a situation where the net worth and capital of the corporation is equal to about one-half of the assets on the one hand, and a situation, on the other, where there is a standby agreement.

Mr. Jones: I will object to that on several grounds. First, it is incompetent, irrelevant and immaterial; second, assuming a set of facts not in evidence; there is no showing that they went into this application at all, or that it was the basis of this loan.

The Court: I will sustain the objection.

Mr. Marcussen: Your Honor, this is a standby agreement; it does not assume any facts in evidence; I am merely calling his attention to it.

The Court: Go ahead and ask him the question.

Mr. Marcussen: I have asked him a question with [631] respect to the comparative positions.

The Court: And then you go on and say what the comparative position is.

Mr. Marcussen: No; I am asking him as an expert.

The Court: Go ahead and ask him.

A. The question was not very clear.

Mr. Marcussen: Will you read the question to the witness?

(Testimony of James H. Cruickshank.)

(Whereupon the last question was read aloud by the reporter as above recorded.)

Q. (By Mr. Marcussen): Do you understand the question?      A. I am afraid I do not.

Q. Where a corporation is organized and has \$187,000 of capital stock paid in, and has no other net worth; with assets of \$2,000,000; or has a net worth, in any event, which is less than one-half of its total assets; in such case, what procedures are used, and what is the practice of the RFC in protecting itself on loans that they may make to such a corporation?

Mr. Jones: That is assuming the RFC sets up such a standard.

The Court: If they have such a standard? Do they have such a standard?

The Witness: Where it is necessary we will have a [632] standby agreement.

The Court: In a case of this kind, you deem it necessary, or did deem it necessary?

The Witness: Yes.

The Court: All right. You can go ahead and answer the question. I will overrule the objection.

Q. (By Mr. Marcussen): Would you deem it necessary to protect yourself?      A. Yes.

Q. You deem it necessary to take such precaution to protect the RFC loan in a situation such as I have described?      A. Yes.

Q. Will you state what those practices are of the RFC?



(Testimony of James H. Cruickshank.)

A. Where an advance is made to strengthen the position of the company in the form of a loan?

Q. Strengthen the position of the company from the point of view of the RFC, or strengthen the position of the loan, when a loan is made by the RFC?

A. What do you want now?

Q. What steps are taken by the RFC in making a loan to a company having a ratio of net worth and assets as I have described them to you?

A. We might suggest that they pay in more capital, or put in more surplus; or the third way to get advances would be made in the form of a standby agreement, if we think the [633] financial structure should be strengthened; we feel we are protected by a standby agreement just the same as though it were capital stock because it is subordinate to our loan.

Q. And are Exhibits C and D such as are generally used by the RFC?

Mr. Jones: We don't care about what is generally done. The question is, what was done.

The Court: Is that what was done?

Mr. Jones: He is putting it on general grounds, asking what the general practice is.

Q. (By Mr. Marcussen): These are the standby agreements that you used in this case?

A. Yes.

The Court: You don't have to ask him that if it has been stipulated.

Mr. Marcussen: It has not been stipulated.



(Testimony of James H. Cruickshank.)

Mr. Jones: But they are in evidence.

Q. (By Mr. Marcussen): I will hand you Respondent's HH for identification and ask you to state what that is (hands document to witness)?

A. The Agency Examiner's report on business application.

Q. For what corporation?

A. For Oregon Electric Steel Rolling Mills.

Mr. Marcussen: If Your Honor please, I would like [634] to offer that in evidence at this time.

The Court: Is there any objection?

Mr. Jones: I don't know; I will have to look at it.

Mr. Marcussen: May I ask counsel if he is going to object?

Mr. Jones: We are going to object.

Mr. Marcussen: Then I will identify it further.

Q. (By Mr. Marcussen): Will you state what the practice is for the preparation of this report by the RFC, and particularly the reason and how they are prepared?

A. The reason, of course, that they are prepared is to assemble the facts to present the same for the approval of loans. What was the other question.

Q. What is the source of the information that is contained in the report?

A. It is based on information received in a loan application prepared by the applicant, by supplemental information received from other sources,

(Testimony of James H. Cruickshank.)

banks, trade, Dun and Bradstreet, or further information received from the applicant subsequent to the date of application.

The Court: Received by whom?

The Witness: By the Examiner in the Loan Agency. [635]

Q. (By Mr. Marcussen): Is that information received, in part, in conference with the applicant after the filing of the application?

A. Yes, many times it is; as a general rule, it is.

Q. Are all those things in the usual course of business gone over with the applicant before the final preparation of the report?

A. That is correct.

Mr. Marcussen: I think that sufficiently identifies it.

Mr. Jones: I notice the heading here "confidential." There is information in there that the applicant knows nothing about.

The Witness: That is true.

Mr. Jones: And he doesn't even know the source of that information?

The Witness: That is true.

Mr. Jones: And the applicant has not signed it, and it was never submitted to him first?

The Witness: That is true.

Mr. Jones: We object to it, based on information or sources unknown to the Petitioner in this case; we object to it as incompetent, irrelevant and immaterial.

(Testimony of James H. Cruickshank.)

The Court: I will sustain the objection.

Q. (By Mr. Marcussen): Was the RFC loan in this case—will you state on [636] what document or documents the RFC loan in this case was granted?

A. I don't understand the question.

Q. On the basis of what document was final approval for the RFC loan made in this case?

A. According to the usual practice.

Q. On what document?

A. You mean on the basis of the application?

Q. Or any other document? Was it on this document, the Examiner's report?

A. Yes, that is correct.

Q. And the application, also, which is already in evidence in this proceeding? A. Yes.

Q. And from time to time, after the application for a loan is received, is it necessary for the RFC, in the course of its usual practice to obtain additional information?

A. After the loan is granted?

Q. No; after the application is filed?

A. In most instances, it is necessary.

Q. Is there usually a considerable lapse of time between the filing of the application and the preparation of the Agency Examiner's report?

A. Well, that varies; sometimes it drags on quite a while; it depends on how difficult it is to get information.

Q. Sometimes is there a considerable lapse of time [637] between the filing of the application and the final approval of a loan? A. Yes.

(Testimony of James H. Cruickshank.)

The Court: What is the date of this document?

Mr. Marcussen: The date of the report, if Your Honor please, that is, this document, Respondent's HH for identification is December 10, 1941.

The Court: On what date was the loan granted? Does the stipulation show?

Mr. Marcussen: Yes. I think the evidence does, also.

Mr. Jones: December 15, 1942.

Q. (By Mr. Marcussen): Do you know when the application itself was granted and approved.

A. I think it was sometime in April, 1942.

Mr. Marcussen: I think there is a resolution on file, one of the Respondent Exhibits, which shows the granting of the loan.

Q. (By Mr. Marcussen): Is final approval of the loan granted in Washington?

A. At that time, most loans were. At the present time, the local agency has authority to make loans up to \$100,000; everything above that goes to Washington.

Q. At this time everything went to Washington, in 1942? A. Yes. [638]

Q. What is the source of the information, or most of the information contained in the Examiner's report?

Mr. Jones: If the Court please, he has been all over that once.

Mr. Marcussen: I am trying to qualify it. It seems to me I should have to qualify that.



(Testimony of James H. Cruickshank.)

A. From the application, from information subsequently received from the applicant, from information received from a credit agency or bank, or different sources from which we could get the information.

Q. (By Mr. Marcussen): Now, with respect to all pertinent information that comes from the applicant or his representative, is that information contained in the Examiner's report?

A. That is right.

Mr. Marcussen: Now, if Your Honor please, I submit here is an application which is already in evidence, which makes certain preliminary representations, or contains preliminary representations by the applicant for a loan.

The Court: What is the date of the application?

Mr. Marcussen: The date of the application is October 29, 1941; and this is the Examiner's report.

The Court: I will overrule the objection.

Mr. Marcussen: Very well.

Mr. Jones: May I save an exception to that?

The Court: Yes.

Mr. Jones: That was based on my original grounds.

The Court: Yes. That will be marked as Respondent's HH.

(The document referred to was marked and received in evidence as Respondent's Exhibit HH.)

Q. (By Mr. Marcussen): I now hand you Re-



(Testimony of James H. Cruickshank.)

spondent's P, which is in evidence in this case, which is the application of the Oregon Electric Steel Rolling Mills for a loan, to the RFC, and I direct your attention to Exhibit E, page nine of that application, which bears the heading of "current financial statement," and under that it states pro forma as of the date the mill is completed, and I ask you to state for the benefit of the judge what that statement is?

A. In connection with the applications, made of new enterprises, we ask that they submit a pro forma financial statement to give us an idea what the financial structure will be like when the organization is completed. In a going established concern it is different. In a new concern, they cannot give a financial statement, so it is projected into the future.

Q. On the application, the pro forma statement—is that pro forma statement supplied by the applicant? A. Yes. [640]

Q. I hand you Respondent's HH which is the Examiner's report dated December 10, 1941, and I call your attention to page 4 of that document, and the pro forma statement contained on that page, and I ask you where the information was secured on the basis of which that statement was made up?

A. I don't know, because I was not assigned to it; this application was not assigned to me.

Q. What is the practice of the RFC in obtaining information on which estimated pro forma statements are gathered for the Examiner's reports?

(Testimony of James H. Cruickshank.)

A. That would naturally have to be secured from the applicant.

Mr. Jones: I move to strike the question and answer. The answer is not responsive.

The Court: He asked you what the practice was; it is secured from the applicant.

The Witness: That is correct, sir.

The Court: The objection is overruled.

Mr. Marcussen: I think that for the most part the document speaks for itself. That is all I wanted to clear up.

The Court: Do you have any further questions?

Mr. Marcussen: That is all.

The Court: Does Petitioner's counsel have any cross-examination? [641]

Mr. Jones: This is a very technical document, and I am not too much informed about it, not sufficiently to examine the witness on it immediately. I would like to have five minutes to consult with an accountant before cross-examining.

The Court: We will take a five minute recess.

(Whereupon a five minute recess was taken.)

The Court: You may proceed, Mr. Jones.

#### Cross-Examination

By Mr. Jones:

Q. I am not sure I understood one point in your testimony. You said something to this effect, that if a corporation has assets of \$2,000,000 and a net worth of \$1,000,000, the capital stock and

(Testimony of James H. Cruickshank.)

surplus, I mean, at \$1,000,000, what kind of a loan would you make?

Mr. Marcussen: I will object to the question on the ground that he didn't testify to that.

Mr. Jones: I am trying to find out.

The Witness: I don't think I did.

Q. (By Mr. Jones): What was your testimony along that line?

A. I think the question that was asked was what capital should a concern have, in my opinion, if the total assets were \$2,000,000. I believe that was the question.

Q. Assuming that was the question and answer, for what [642] purpose would you say it should have that amount of capital and surplus?

A. I think it is generally agreed that the incorporators or the owners of the business should have as much or more in it than the creditors.

Q. Let me ask you this: During the war, did you hold people to that ratio in making RFC loans?

A. Not entirely.

Q. As a matter of fact, on this very loan, on this pro forma statement, the total assets were \$890,000, weren't they? A. Yes.

Q. And the net worth of the company was stated pro forma as \$250,000?

A. That was in the application.

Q. That is the pro forma statement in the application?

A. Yes. The loan was not based on that.

(Testimony of James H. Cruickshank.)

Q. As a matter of fact, when you finally made the loan, there was not this much actual capital, was there? A. That is true.

Q. And you made a loan of \$700,000 on issued capital of \$187,000? A. Yes.

Q. You knew that was the issued stock at the time you made it? A. Yes. [643]

Q. There was no misunderstanding on your part?

A. That's right.

Q. Now, you spoke a good deal about standby creditors. Actually, the standby creditors position is governed by a standby agreement? A. Yes.

Q. It may mean one thing in one case and another thing in another? A. That is right.

Q. It may mean one thing for one kind of a debt, and another thing for another kind of a debt?

A. That's right.

Q. But, in the final analysis, the standby governs what the position is of the creditor with respect to other creditors; is that right?

A. Yes.

Q. Is there any payment being made on that loan? Are there any payments being made on that loan by the Oregon Steel? A. Yes.

Q. And the capital stock is still \$187,000; that is, the issued capital stock?

A. That's right.

Q. And it is accumulating a surplus, is it not?

A. That is right. [644]

Q. So that, even with the RFC, you don't hold



(Testimony of James H. Cruickshank.)

rigidly to any fixed formula in the ratio of assets to net worth?

A. No; I think I said "as a general rule."

Q. Circumstances alter cases? A. Yes.

Q. And the war situation altered many cases didn't it? A. Yes.

Mr. Jones: That is all. Thank you very much.

### Redirect Examination

By Mr. Marcussen:

Q. Mr. Cruickshank, I have just a few questions. In this case, why was the RFC willing to advance such a loan with only \$187,000 paid in capital?

Mr. Jones: That was gone over on direct examination thoroughly.

Mr. Marcussen: No, it was not. It is simply in response to a question that counsel has asked on cross-examination.

The Court: I will overrule the objection.

The Witness: Shall I answer the question?

Q. (By Mr. Marcussen): Yes.

A. We had in that case,—there were advances made, covered by the standby agreement, which, I believe, I stated before, we were satisfied to take in lieu of paid in capital [645] stock.

### Recross-Examination

By Mr. Jones:

Q. By that you mean, Mr. Cruickshank, that the creditors, the Alaska Junk Company, on whatever



(Testimony of James H. Cruickshank.)

the Oregon Steel owed them, without trying to tie any name on the accounts or the type of obligation, but whatever the obligation of Oregon Steel was to Alaska?

A. I don't know that I understand you.

Q. Without trying to tie any name on the account or the type of obligation, whatever the obligation of Oregon Steel was to Alaska, you felt that you were protected in having the Alaska Junk stand by with respect to certain other assets? Is that correct?

A. That is right.

Q. You had some prior rights?

A. That is right.

Q. You are not trying to catalogue that as capital stock, or anything else?

A. That's right.

Q. That standby agreement just gave you a prior position?

A. That's right.

Mr. Jones: That is all.

Mr. Marcussen: That's all.

The Court: You may stand aside. [646]

(Witness excused.)

The Court: Call your next witness.

Whereupon,

W. P. GREY

recalled as a witness by and on behalf of the Respondent, having been previously sworn, was further examined and testified as follows:

The Court: The Court is not going to tolerate

(Testimony of W. P. Grey.)

calling witnesses back from cross-examination, unless there is some reason for it.

Mr. Marcussen: Permission was granted to recall this witness to clarify one point.

The Court: Oh, yes, but please avoid it. It is a bad habit that you want to avoid.

### Direct Examination

By Mr. Marcussen:

Q. I call your attention to the last paragraph on page 9 on the Dun and Bradstreet of July, 1947, concerning the Wolf and Schnitzer Machinery Company, or the Alaska Junk, and I call your attention to the following sentence in the last paragraph which was read in evidence this morning: "At December 31, 1942, advances from the predecessor to that former related concern totaled approximately \$572,000, such advances being subsequently extended to approximately \$75,000."

A. It should have been \$750,000. There is a typographical [647] error there.

Q. Calling your attention to the first part of the sentence, what is meant by the phrase "predecessor to that former related concern"?

A. The predecessor is the four partners, Mr. Schnitzer, Mr. Wolf, and their wives.

Q. What is the "former related concern"?

A. The former related concern,—this analysis here is related to this partnership, which was changed in the history. It was changed to this partnership here (indicating).

(Testimony of W. P. Grey.)

Q. When you say "this partnership" you mean the Schnitzer and Wolf Machinery Company?

A. That is simply the style.

The Court: The only purpose for which he was to be recalled, was to show whether it was a typographical error there in showing \$75,000 instead of \$750,000.

Mr. Marcussen: The entire sentence was negative. Therefore it was all in question.

The Court: The Court will excuse the witness. He has answered that question.

Mr. Marcussen: May I have an exception?

The Court: You may have an exception.

(Witness excused.)

Mr. Marcussen: If Your Honor please, the Respondent rests. [648]

\* \* \*

The Tax Court of the United States

T. C. Docket No. 14208

SAM SCHNITZER,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14209

HARRY J. WOLF,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14278

MONTE L. WOLF,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14279

BLOSSOM M. GOLDSTEIN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14280

CHARLOTTE C. COHON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

T. C. Docket No. 14372

ESTATE OF JENNIE WOLF, Deceased, by  
Harry J. Wolf, Administrator de bonis non of  
said estate with will annexed, and by Harry J.  
Wolf, former executor of said estate,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

## STIPULATION

It is hereby stipulated and agreed by and between the parties hereto, by their respective counsel, that for the purposes of these proceedings the following facts are admitted and shall be taken as true, without prejudice to the right of either party to present other and further evidence not inconsistent with the facts herein stipulated to be taken as true, and the right of either party to argue on brief the question of the materiality of any of the facts herein set forth. All exhibits referred to herein are submitted herewith, made a part hereof and shall be received



in evidence unless objection is made and sustained to the admission of any exhibit on the ground of its relevancy, and/or materiality.

1. The returns for the years 1942 and 1943 herein involved were filed by petitioners Sam Schnitzer, Harry J. Wolf and petitioner's decedent, Jennie Wolf, with the Collector for the District of Oregon on the cash and calendar year basis.

2. During the years 1942 and 1943, Alaska Junk Company, hereinafter sometimes called Alaska Junk, a co-partnership, kept its books and made its returns on the accrual and calendar year basis.

3. Petitioner Harry J. Wolf died on February 6, 1948. Monte L. Wolf, his son, is the duly appointed, qualified and acting executor of the will and estate of said Harry J. Wolf, deceased. The said estate by Monte L. Wolf, Executor, may be substituted as the petitioner in proceeding, Docket No. 14209.

4. Prior to his death, petitioner Harry J. Wolf was the duly and regularly appointed executor of the estate of his wife, Jennie Wolf, deceased. After the said estate was closed and Harry J. Wolf discharged as said executor, said estate was reopened by proper order of court and by said order Harry J. Wolf was duly appointed the administrator de bonis non with the will annexed of said estate and was duly authorized to institute the proceeding at Docket No. 14372. Harry J. Wolf qualified as said administrator and acted in such capacity until his

death. After his death his son, Monte L. Wolf, succeeded him as such administrator. The above proceeding may accordingly be prosecuted by him.

5. Petitioner Sam Schnitzer and Rose Schnitzer were intermarried in Portland, Oregon, in 1906, and ever since have been and now are husband and wife. Petitioner Harry J. Wolf and petitioner's decedent Jennie Wolf were intermarried at Portland, Oregon, June 16, 1906, and were husband and wife at all times from said date until the death of Jennie Wolf on April 8, 1945.

6. Petitioners Monte L. Wolf, Blossom M. Goldstein and Charlotte C. Cohon are the children of petitioner Harry J. Wolf and petitioner's decedent, Jennie Wolf. At the time of her death Jennie Wolf was the owner of property and assets of the then fair market value in excess of the deficiency asserted by the respondent against her estate in the proceeding, Docket No. 14372. The above-named children of Jennie Wolf were the distributees of the residuary assets of her estate and as such distributees each received on or about April 1, 1946, from said estate, property and assets having a fair market as follows:

Monte L. Wolf.....	\$22,923.09
Blossom M. Goldstein.....	\$23,855.57
Charlotte C. Cohon.....	\$24,112.08

After the distribution of said property and assets to said children, said estate was left without any means whereby any deficiency which this Court may

determine against the Estate of Jennie Wolf might be paid. By reason of the distribution of said property and assets of the Estate of Jennie Wolf, as aforesaid, each of the petitioners Monte L. Wolf, Blossom M. Goldstein and Charlotte C. Cohon became liable at law and in equity to the extent of amount set forth above opposite his or her name for the payment of any deficiency which may in these proceedings be finally determined against the Estate of Jennie Wolf for the taxable years herein involved with interest as provided by law.

7. During the years 1942 and 1943 Alaska Junk was engaged in the business of buying, selling and generally dealing in junk, new and second-hand pipe, tools, machinery, hardware, scrap and new metal and metal products of every character. Its principal place of business was in Portland, Oregon.

8. Exhibit 1 is a copy of a document executed on January 3, 1928, by petitioners Sam Schnitzer and Harry J. Wolf, and their wives Rose Schnitzer and Jennie Wolf.

9. Exhibit 2 is a copy of the Assumed Business Name Certificate which the partners of Alaska Junk filed with the Recorder of Conveyances of Multnomah County, Oregon, January 3, 1928. Said certificate was recorded in the Record of Assumed Business Names of said county and state on January 3, 1928, in Book 16 at page 140 thereof, and no document in any way modifying, changing or cancelling the effect or terms of said certificate was

made or filed prior to the end of the calendar year 1943.

10. Petitioners Sam Schnitzer and Harry J. Wolf each draw a salary of \$10,000.00 in each of the years 1942 and 1943 from Alaska Junk, which salaries were deducted as business expenses of the partnership prior to any division of the remaining profits between the partners. Rose Schnitzer and Jennie Wolf did not draw salaries from Alaska Junk.

11. Oregon Electric Steel Rolling Mills (hereinafter sometimes called Oregon Steel), an Oregon corporation, was organized June 4, 1941. Its authorized capital consisted of 2,500 shares of a par value of \$100.00 per share. Exhibit 3 is a photostatic copy of the subscriptions to the capital stock of Oregon Steel. Certificates for shares in the capital stock of Oregon Steel were issued and transferred as shown below in this and subsequent paragraphs hereof. Said stock was paid for on the dates shown in Exhibit 9.

Date	Cert. No.	Name	No. of Shares
June 12, 1941	1	Morris Schnitzer	1
June 12, 1941	2	Sam Schnitzer	1
June 12, 1941	3	Harry J. Wolf	1
June 12, 1941	4	Bernard Levin	1
June 12, 1941	5	Louis Schnitzer	1
Aug. 4, 1941	6	L. N. Rosenbaum	1
Feb. 10, 1942	7	Morris Schnitzer	1251
Feb. 10, 1942	8	Sam Schnitzer	312½
Feb. 10, 1942	9	Harry J. Wolf	312½

12. Certificate No. 1 was surrendered by Morris Schnitzer, and the share represented thereby was



included in the above-mentioned Certificate No. 7. Certificate No. 2 was surrendered by Sam Schnitzer, and the share represented thereby was included in the above-mentioned Certificate No. 8. Certificate No. 3 was surrendered by Harry J. Wolf, and the share represented thereby was included in the above-mentioned Certificate No. 9. Certificate No. 5 was surrendered by Louis Schnitzer, and the share represented thereby was reissued to L. N. Rosenbaum, and was represented by the above-mentioned certificate No. 6.

13. Certificates numbered 8 and 9 were surrendered by Sam Schnitzer and Harry J. Wolf, and the shares represented thereby were reissued as follows:

Date Issued	Cert. No.	Name	No. of Shares
Feb. 10, 1942	10	Rose Schnitzer	156 $\frac{1}{4}$
Feb. 10, 1942	11	Sam Schnitzer	156 $\frac{1}{4}$
Feb. 10, 1942	12	Jennie Wolf	156 $\frac{1}{4}$
Feb. 10, 1942	13	Harry J. Wolf	156 $\frac{1}{4}$

14. Certificate No. 7 was surrendered by Morris Schnitzer, and the shares represented thereby were reissued as follows:

Date Issued	Cert. No.	Name	No. of Shares
March 11, 1943	14	Morris Schnitzer	625
March 11, 1943	15	Sam Schnitzer	157 $\frac{1}{4}$
March 11, 1943	16	Rose Schnitzer	156 $\frac{1}{4}$
March 11, 1943	17	Harry J. Wolf	157 $\frac{1}{4}$
March 11, 1943	18	Jennie Wolf	156 $\frac{1}{4}$
March 11, 1943	19	Monte Wolf	1



15. After the last reissuance to November 26, 1943, the issued stock of said corporation was owned as follows:

Cert. No.	Name	No. of Shares
10, 16	Rose Schnitzer	312½
11, 15	Sam Schnitzer	313½
12, 18	Jennie Wolf	312½
13, 17	Harry J. Wolf	313½
14	Morris Schnitzer	625
19	Monte Wolf	1
		<hr/>
		1878

16. Exhibit 4 is a copy of the minutes of a special meeting of the Board of Directors of Oregon Steel held on January 12, 1943, at Portland, Oregon.

17. On or about January 12, 1943, 249 debentures, each in the sum of \$1,000.00 and entitled "First Debenture, Oregon Electric Steel Rolling Mills," were issued by Oregon Steel in the total amount of \$249,000.00, as follows:

Debenture Numbers	Recipient	Amount
1- 75, incl.	Morris Schnitzer .....	\$ 75,000.00
76-119, incl.	Sam Schnitzer .....	\$44,000.00
120-162, incl.	Rose Schnitzer .....	43,000.00
163-206, incl.	Harry J. Wolf .....	44,000.00
207-249, incl.	Jennie Wolf .....	43,000.00
		<hr/>
Total.....		\$249,000.00

All said debentures were accepted by said persons to whom issued.

18. Exhibit 5 is a conformed copy of debenture numbered 201, issued to and accepted by Harry J. Wolf. All of the other above-mentioned debentures were identical in form, bore the same date and were

executed by Oregon Steel in exactly the same manner as said Exhibit No. 5, except for the fact that they bore different numbers.

19. Exhibit 6 consists of photostatic copies of pages J13, J22, J23 and J24 of the Journal of the Alaska Junk Company for the year 1943.

20. July 14, 1943, the Stocks and Bonds account of the Alaska Junk in its general ledger was charged with the sum of \$174,000.00 for said debentures issued to Sam Schnitzer, Rose Schnitzer, Harry J. Wolf and Jennie Wolf, and with the sum of \$125,200.00 for the shares of stock in Oregon Steel issued to said persons.

21. Exhibit 7 is photostatic copies of four journal entries made by and on the records of Oregon Steel.

22. Exhibits 8, 9 and 10 are, respectively, photostatic copies of the Unissued Capital Stock, Stock Subscriptions and Capital Stock accounts of Oregon Steel in its general ledger.

23. Exhibit 11 is a photostatic copy of the Debentures Payable account of Oregon Steel in its general ledger.

24. Exhibit 12 is a photostatic copy of a page in the general ledger of Oregon Steel, showing its Mortgage Payable account with the Reconstruction Finance Corporation (sometimes hereinafter called RFC), from the opening of said account to November 30, 1943.

25. On December 15, 1942, Oregon Steel executed and delivered to RFC a promissory note in the sum of \$700,000.00, a copy of which is marked Exhibit 13. On the same date in order to secure the payment of said promissory note Oregon Steel executed and delivered to RFC a mortgage upon its real property and upon certain personal property described therein. Said mortgage was duly recorded on December 17, 1942, in the Record of Mortgages for Multnomah County, Oregon. Exhibit 14 is a copy of said mortgage.

26. Exhibit 15 is a photostatic copy of the Notes Payable account in the general ledger of Oregon Steel for the year 1943 and a part of the year 1944. The balance in said account on November 26, 1943, was \$145,499.71. The payment of all the notes recorded in said account was secured by a pledge of the inventories and accounts receivable of a value in excess of said balance due on said notes. The notes in this account were payable to banks. The RFC note described in paragraph 25, above, was not included in said account nor were there included therein any notes payable to any of Oregon Steel stockholders.

27. At and during all times hereinafter mentioned, Morris Schnitzer was engaged in the business of buying and selling new and used iron, steel, tools and machinery in Portland, Oregon, and conducted such business under the name and style of Schnitzer Steel Products Co. Exhibit 16 consists

of photostatic copies of seven pages in the general ledger of Oregon Steel, showing its account with Schnitzer Steel Products Co.

28. Exhibit 17 consists of photostatic copies of five pages in the general ledger of Oregon Steel showing its general account with Alaska Junk.

29. Exhibit 18 is a photostatic copy of the page of the general ledger of Oregon Steel showing its account of scrap metal purchased from Alaska Junk.

30. Exhibit 19 is a balance sheet of Oregon Steel reflecting the accounts in its books as at October 31, 1943.

31. On November 26, 1943, Oregon Steel executed and delivered to Alaska Junk a promissory note in the amount of \$427,843.87 as evidence of the advances made to it by Alaska Junk as of that day, shown by the books of Oregon Steel. Exhibit 20 is a photostatic copy of said note. On the same day, Oregon Steel executed and delivered to Schnitzer Steel Products Co. a promissory note in the amount of \$26,829.28 as evidence of the advances made to it by Morris Schnitzer (who did business under the assumed name and style of Schnitzer Steel Products Co.) as shown by the books of Oregon Steel on said date. Exhibit 21 is a photostatic copy of the last-mentioned promissory note.

32. On November 26, 1943, Sam Schnitzer, Rose Schnitzer, Harry J. Wolf, Jennie Wolf and Morris



Schnitzer sold all their stock in Oregon Steel to Kenneth E. Hall and A. M. Mears for the sum of one cent per share. After said sale and on said day, the directors of the said corporation held a special meeting in Portland, Oregon. Exhibit 22 is a copy of the minutes of said meeting.

33. On November 26, 1946, pursuant to the authority contained in said minutes, Oregon Steel executed and delivered to Sam Schnitzer, Rose Schnitzer, Harry J. Wolf, Jennie Wolf and Morris Schnitzer a promissory note for \$249,000.00, and another promissory note for \$151,000.00, to secure the payment of which it also executed on the same day and pursuant to the same authority a second mortgage in the amount of \$249,000.00, and a third mortgage in the amount of \$151,000.00, upon its real property and certain personal property described in the mortgages. Exhibits 23 and 24 are copies of the said mortgages, each of which contains a copy of the note for the payment of which it was given as security.

34. The first promissory note and second mortgage securing the payment of the same were delivered and accepted in exchange for the debentures mentioned in paragraph 17. Exhibit 25 is a copy of the receipt for payment of said debentures, which were returned to Oregon Steel as fully paid.

35. The second promissory note and third mortgage securing the same were given and accepted in exchange for the promissory notes referred to above



in paragraph 31 hereof, which notes were thereupon each marked upon the face as follows: "Compromised and Cancelled in consideration of delivery of third mortgage." Said notes were then returned to Oregon Steel as fully paid.

36. Exhibit 26 is the general account of Oregon Steel on the books of Alaska Junk showing entries from October 22, 1941, to December 31, 1943.

37. Exhibit 27 is the account of Oregon Steel on the books of Alaska Junk for scrap furnished by Alaska Junk to Oregon Steel showing entries beginning July 22, 1943, through December 14, 1943.

38. Exhibit A is a copy of a Guaranty Agreement dated December 15, 1942, executed in favor of RFC by Morris Schnitzer, Sam Schnitzer, Rosie Schnitzer, Harry J. Wolf and Jennie Wolf.

39. Exhibit B is a copy of a Loan Agreement dated December 15, 1942, executed by Oregon Steel through its president Morris Schnitzer in favor of RFC.

40. Exhibit C is a copy of a Standby Agreement dated December 15, 1942, executed by Oregon Steel through its president, Morris Schnitzer, in favor of RFC and signed by standby creditors Morris Schnitzer, Sam Schnitzer, Harry J. Wolf and Monte Wolf.

41. Exhibit D is a copy of a Standby Agreement dated December 26, 1942, executed by Oregon Steel through its president, Morris Schnitzer, in

favor of RFC and signed by Alaska Junk Company, standby creditor, through its general partners, Sam Schnitzer and Harry J. Wolf.

42. Exhibit E is a copy of a resolution adopted by the Executive Committee of RFC on April 2, 1942, pertaining to the granting of a loan to Oregon Steel in the original amount of \$600,000.00.

43. Exhibit F is a copy of the same resolution referred to above in paragraph 42 showing various amendments made from time to time as therein indicated.

44. Exhibit G is a copy of a resolution adopted by the Executive Committee of RFC on December 2, 1942, amending the aforesaid resolution adopted by RFC on April 2, 1942.

45. Exhibit H is a copy of a resolution adopted by the Executive Committee of RFC on December 4, 1942, amending the aforesaid resolution adopted by RFC on April 2, 1942.

46. Exhibit I is a copy of a resolution adopted by the Board of Directors of RFC on December 8, 1942, amending the aforesaid resolution adopted by RFC on April 2, 1942.

47. Exhibit J is a copy of a resolution adopted by the Board of Directors of RFC on November 25, 1943, pertaining to the loan made by RFC to Oregon Steel, and sale to Mears and Hall.

48. Exhibit K is a copy of the minutes of a

special meeting of the Board of Directors of Oregon Steel held on October 27, 1941.

49. Exhibit L is a copy of the minutes of an annual meeting of the Directors of Oregon Steel held on August 10, 1942.

50. Exhibit M is a copy of the minutes of a special meeting of the Board of Directors of Oregon Steel held on December 15, 1942.

51. Exhibit N is a copy of the minutes of a special meeting of the Board of Directors of Oregon Steel held on May 17, 1943.

/s/ ROBT. T. JACOB,

Counsel for Petitioners.

/s/ CHARLES OLIPHANT,

Chief Counsel, Bureau of Internal Revenue, Counsel for Respondent.

[Endorsed]: Filed June 11, 1948.

[Title of Tax Court and Causes.]

ORDER RE TRANSMISSION OF  
ORIGINAL EXHIBITS

Upon motion of counsel for petitioner, it is

Ordered: That the Clerk of The Tax Court of the United States shall transmit Petitioner's Original Exhibits 1-27, inclusive, 28, 30, 31, 33-36, inclusive, 65, 66, 72-79, inclusive; Respondent's Exhibits A-Z, AA-HH, inclusive, as requested in the Designation of Record, 15 days prior to the hearing of the above-entitled proceedings upon the advice of counsel of either party, to the Clerk of the Ninth Circuit, with the request that he safely keep and return said exhibits to the Clerk of this Court upon final determination in the U. S. Court of Appeals for the Ninth Circuit.

[Seal]      /s/ JOHN W. KERN,  
                                 Judge.

Dated: Washington, D. C., January 19, 1950.

In the United States Court of Appeals  
for the Ninth Circuit.

T. C. Docket No. 14208

SAM SCHNITZER,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

T. C. Docket No. 14209

ESTATE OF HARRY J. WOLF, Deceased, by  
MONTE L. WOLF, Administrator de bonis  
non with the will annexed of said Estate,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

T. C. Docket No. 14278

MONTE L. WOLF,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.



T. C. Docket No. 14279

BLOSSOM M. GOLDSTEIN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14280

CHARLOTTE C. COHON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14372

ESTATE OF JENNIE WOLF, Deceased, by  
MONTE L. WOLF, Administrator de bonis  
non with the will annexed of said Estate,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

## DESIGNATION OF RECORD

To: The Clerk of the Tax Court of the United  
States:

Petitioners and each of them hereby designate  
that the following portions of the record, proceed-

ings and evidence in these cases be contained in the record on appeal to the United States Court of Appeals for the Ninth Circuit:

1. All Petitions and Amendments to Petitions.
2. All Answers and Amendments to Answers.
3. All Replies.
4. Findings of Fact, Opinions and Decisions of the Tax Court.
5. Petition for Review of the decisions of the Tax Court together with Notice of Filing of Petition for Review in each of said proceedings.
6. Transcript of Proceedings before the Tax Court.
7. Stipulation.
8. a. Petitioner's original Exhibits 1-27 inclusive, 28, 30, 31, 33-36 inclusive, 65, 66, 72-79 inclusive;  
b. All of Respondent's original Exhibits, designated A-Z, AA-HH inclusive.
9. This Designation of Record.
10. Order to send original papers and exhibits

to the Clerk of the United States Court of Appeal for the Ninth Circuit.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES.

Personal service of the foregoing Designation of Record is hereby acknowledged this 10th day of January, 1950.

/s/ CHARLES OLIPHANT,

Chief Counsel, Bureau of Internal Revenue, Counsel for Respondent.

[Endorsed]: Filed Jan. 9, 1950.

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The Tax Court of the United States  
Washington

Docket No. 14208

SAM SCHNITZER,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

### CERTIFICATE

I, Victor S. Mersch, Clerk of The Tax Court of the United States do hereby certify that the foregoing documents, 1 to 13, inclusive, constitute and are all of the original papers and proceedings before The Tax Court of the United States as set forth

in the "Designation of Record" except the original exhibits 1-27 incl., 28, 30, 31, 33-36 incl., 65, 66, 72-79 incl.; A-Z, AA-HH incl., on file in my office as the original record in the proceeding and in which the petitioner in The Tax Court proceeding has initiated an appeal as above numbered and entitled, together with a true copy of the docket entries in said Tax Court proceeding, as the same appear in the official docket book in my office.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia, this 23rd day of January, 1950.

[Seal]      /s/ VICTOR S. MERSCH,  
Clerk, The Tax Court of the United States.

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[Endorsed]: No. 12471. United States Court of Appeals for the Ninth Circuit. Sam Schnitzer, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of Record. Petition to Review a Decision of The Tax Court of the United States.

Filed February 7, 1950.

/s/ PAUL P. O'BRIEN,  
Clerk of the United States Court of Appeals for  
the Ninth Circuit.

In the United States Court of Appeals  
for the Ninth Circuit

T. C. Docket No. 14208

SAM SCHNITZER,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

T. C. Docket No. 14209

ESTATE OF HARRY J. WOLF, Deceased, by  
MONTE L. WOLF, Administrator de bonis  
non with the will annexed of said Estate,  
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

T. C. Docket No. 14278

MONTE L. WOLF,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.



T. C. Docket No. 14279

BLOSSOM M. GOLDSTEIN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14280

CHARLOTTE C. COHON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14372

ESTATE OF JENNIE WOLF, Deceased, by  
MONTE L. WOLF, Administrator de bonis  
non with the will annexed of said Estate,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

### MOTION TO CONSOLIDATE APPEALS

The above named petitioners on review and each of them, acting by and through their attorneys of record, hereby move this court to consolidate the

above entitled proceedings for purposes of the printed record on appeal, the briefing, the hearing, the argument, the decision and for all other purposes connected with the final disposition of said proceedings on review.

This motion is based on the grounds that all of the above entitled proceedings were consolidated for trial below in the Tax Court, that the Tax Court made but one set of findings of fact and rendered but one opinion in connection with all of these cases, that each of these cases involves the same facts, that each of the petitioners on review was either a partner or is now the transferee of a decedent who was a partner in a partnership known as the Alaska Junk Company, that the sole question for decision concerns the deductibility of a bad debt by said Alaska Junk Company, and that the decision on this single point is determinative of the income tax liability of each of said partners or said transferees of partners who are the petitioners herein.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,

917 Public Service Building,  
Portland 4, Oregon.

I, Randall S. Jones, being on oath first duly sworn, depose and say:

That on the 13th day of February, 1950, I served the foregoing Motion to Consolidate Appeals upon Charles Oliphant, Chief Counsel, Bureau of Inter-

nal Revenue of the United States, by on said day depositing a duly certified copy thereof in the United States mails with full postage and registration charges prepaid, addressed to Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, Internal Revenue Building, Washington, D. C. Said papers were deposited in the United States mails at the Federal Post Office, S. W. Sixth and Main Streets, Portland 4, Oregon.

/s/ RANDALL S. JONES.

Subscribed and sworn to before me this 13th day of February, 1950.

[Seal]      /s/ JACQUELINE MOHLAND,  
Notary Public for Oregon.

My commission expires: 9-22-52.

So Ordered:

/s/ WILLIAM DENMAN,  
Chief Judge.

/s/ HOMER BONE,  
/s/ WM. E. ORR,  
U. S. Circuit Judge.

[Endorsed]: Filed Feb. 15, 1950.

[Title Court of Appeals and Causes.]

STATEMENT OF POINTS ON WHICH  
PETITIONERS INTEND TO RELY

The petitioners on review hereby enumerate the points on which they intend to rely on appeal and which are as follows:

1. The Tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the partnership in which petitioners were partners was not a bad debt and not deductible in computing the net income of said partnership and petitioners' net income subject to taxation for the taxable year 1943.

2. The Tax Court erred in holding that the total, or any amount in excess of \$125,000.00, representing bills paid for, cash advanced to, and goods sold to Oregon Electric Steel Rolling Mills by the partnership in which petitioners or their transferors were partners, constituted a contribution to the capital of said Oregon Electric Steel Rolling Mills.

3. The Tax Court erred in not finding and holding that all and every part of said sum of \$202,350.60 was a debt owed to the partnership in which petitioners were partners.

4. The decision entered by the Tax Court herein is contrary to the law, the Tax Court's findings of fact, and the evidence; and is not supported by said findings of fact or the evidence and is in disregard of both said findings of fact and the evidence.

5. The Tax Court erred in failing to include in its findings material facts clearly established by the evidence which further show that the bills paid, cash advanced and goods sold to Oregon Electric Steel Rolling Mills constituted an indebtedness owed to the partnership.

6. The Tax Court erred in admitting respondent's exhibits O, P, Q, U, V, AA, FF, GG and HH over objections of petitioner for the reasons set forth respectively on pages 120, 121, 122, 129, 134, 137, 495, 589-591, 621 and 636, 639 and 640 of the *Report's* Transcript of the Proceedings before said court.

7. The Tax Court erred in receiving oral testimony adduced by respondent over objections of the petitioners as set forth in those portions from the Reporter's Transcript of the Proceedings before said court which the petitioners have designated for inclusion in the Printed Record.

8. The Tax Court erred in sustaining objections of the respondent to questions asked by petitioners and to oral testimony offered by petitioners, which questions, objections and rulings thereon are set forth in those portions from the Reporter's Transcript of the Proceedings before said court which the petitioners have designated for inclusion in the Printed Record.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,

917 Public Service Bldg.,  
Portland 4, Oregon.



I, Randall S. Jones, being on oath first duly sworn, depose and say:

That on the 13th day of February, 1950, I served the Statement of Points on which Petitioners Intend to Rely upon Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, by on said day depositing a duly certified copy thereof in the United States mails with full postage and registration charges prepaid, addressed to Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, Internal Revenue Building, Washington, D. C. Said papers were deposited in the United States mails at the Federal Post Office, S. W. Sixth and Main Streets, Portland 4, Oregon.

/s/ RANDALL S. JONES.

Subscribed and sworn to before me this 13th day of February, 1950.

[Seal]      /s/ JACQUELINE MOHLAND,  
Notary Public for Oregon.

My commission expires: 9-22-52.

[Endorsed]: Filed Feb. 16, 1950.

[Title of Court of Appeals and Causes.]

MOTION TO BE RELIEVED FROM PRINT-  
ING OR REPRODUCING EXHIBITS

Come now the petitioners on review, by their attorneys of record, and respectfully apply to and move the above-entitled court for an order relieving the petitioners on review from printing or reproducing the exhibits in these appeals in the printed transcript of record on appeal, and ordering that all said exhibits be considered by this court in their original form in determining the questions involved in this appeal without such exhibits being so printed or reproduced and as though they were fully set forth in said printed transcript of record. This application is based upon the ground that the exhibits and papers in these proceedings are unusually voluminous and lengthy, comprising hundreds of pages of documents and accounts, many of which cannot be readily printed, and on the further ground that the cost of printing said exhibits and papers would be completely disproportionate to the convenience of having them in their original form.

Pursuant to a similar motion of petitioners heretofore filed in the Tax Court of the United States in which petitioners relied on Rules 11 and 31 of the Rules, Court of Appeals, Ninth Circuit and Rule 75 of the Federal Rules of Civil Procedure,

which rules provide for the preparation of the record on appeal of decisions of the Tax Court of the United States, the Tax Court entered an order that the original exhibits be transmitted to the Clerk of the United States Court of Appeals for the Ninth Circuit fifteen days prior to the hearing of the appeal on the advice of the counsel of either party.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,

917 Public Service Building,  
Portland 4, Oregon.

I, Randall S. Jones, being on oath first duly sworn, depose and say:

That on the 13th day of February, 1950, I served the foregoing Motion to be Relieved from Printing or Reproducing Exhibits upon Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, by on said day depositing a duly certified copy thereof in the United States mails with full postage and registration charges prepaid, addressed to Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, Internal Revenue Building, Washington, D. C. Said papers were deposited in the United States mails at the Federal Post Office,

S. W. Sixth and Main Streets, Portland 4, Oregon.

/s/ RANDALL S. JONES.

Subscribed and sworn to before me this 13th day of February, 1950.

[Seal]      /s/ JACQUELINE MOHLAND,  
Notary Public for Oregon.

My Commission expires: 9-22-52.

So Ordered:

/s/ WILLIAM DENMAN,  
Chief Judge.

/s/ HOMER BONE,

/s/ WM. E. ORR,

United States Circuit Judges.

[Endorsed]: Filed Feb. 16, 1950.

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[Title of Court of Appeals and Causes.]

## DESIGNATION OF RECORD

Petitioners on Review hereby designate the entire record on appeal as material for consideration of the points enumerated in the Statement of Points on Which Petitioners Intend to Rely, to wit:

1. All Petitions and Amendments to Petitions.
2. All Answers and Amendments to Answers.
3. All Replies.
4. Findings of Fact, Opinion and Decisions of the Tax Court.
5. Petition for Review of the decisions of the

Tax Court together with Notice of Filing of Petition for Review in each of said proceedings.

6. All parts of Transcript of Proceedings before the Tax Court relating to the questions involved in this appeal and which parts are as follows:

Beginning on p. 32, line 9, to and including third line from bottom p. 49.

Beginning on p. 57, ninth line from bottom, to and including the 5th line from the bottom of page 175.

Beginning with line 8, p. 187, to and including line 6, p. 195.

Beginning with line 11 from the bottom of page 199 reading "By Mr. Jones," to and including first line page 212 reading "to make that clear."

Beginning on p. 220, "Cross-Examination by Mr. Marcussen" to and including fifth line from bottom, p. 234.

Beginning at the 9th line from the bottom of p. 245, reading "By Mr. Marcussen," to and including bottom, p. 315.

Beginning line 8, p. 320 ("Q. During the time, etc.") to and including sixth line from bottom, p. 352.

Beginning p. 371, third line from bottom, to and including line 11, p. 425.

Beginning top p. 435, to and including fourth line from bottom, p. 435.

Beginning p. 452, line nine, to and including line 6, p. 464.

Beginning top p. 466, to and including line 19, p. 484.



Beginning p. 488 with "Cross-Examination" to and including line 11, p. 501.

Beginning p. 512, line 3, to and including line 4, p. 514.

Beginning p. 525, sixth line from bottom, to and including second line from bottom, p. 648.

7. Stipulation.

8. a. Petitioners' original Exhibits 1-27, inclusive, 28, 30, 31, 33-36, inclusive, 65, 66, 72-79, inclusive;

b. All of Respondent's original Exhibits, designated A-Z, AA, BB, DD, to HH, inclusive.

9. Designation of Record (Tax Court).

10. Order to send original papers and exhibits to the Clerk of the United States Court of Appeals for the Ninth Circuit.

11. Motion to Consolidate Appeals.

12. Order Consolidating Appeals.

13. Motion to be Relieved from Printing or Reproducing Exhibits.

14. Order Relieving Petitioners from Printing or Reproducing Exhibits.

15. Statement of Points on Which Petitioners Intend to Rely.

16. This Designation of Record.

Petitioners on Review, subject to approval by the court of the motion enumerated in 13. above and granting of the order in 14. above, further

designate that petitioners' original exhibits and respondent's original exhibits enumerated in 8.a. and b. above shall not constitute part of the printed transcript of record, but shall be considered in original form.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,

917 Public Service Building,  
Portland 4, Oregon.

I, Randall S. Jones, being on oath first duly sworn, depose and say:

That on the 13th day of February, 1950, I served the Designation of Record upon Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, by on said day depositing a duly certified copy thereof in the United States mails with full postage and registration charges prepaid, addressed to Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, Internal Revenue Building, Washington, D. C. Said papers were deposited in the United States mails at the Federal Post Office, S. W. Sixth and Main Streets, Portland 4, Oregon.

/s/ RANDALL S. JONES.

Subscribed and sworn to before me this 13th day of February, 1950.

[Seal] /s/ JACQUELINE MOHLAND,  
Notary Public for Oregon.

My Commission expires 9-22-52.

[Endorsed]: Filed Feb. 16, 1950.

No. 12472

---

United States  
Court of Appeals  
for the Ninth Circuit.

---

ESTATE OF HARRY J. WOLF, Deceased, by  
Monte L. Wolf, Administrator, de bonis non  
with the will annexed of said estate,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE.

Respondent.

---

Transcript of Record

---

Petition to Review a Decision of the Tax Court  
of the United States

FILED

APR 5 1950

PAUL P. O'BRIEN,  
CLERK



No. 12472

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United States  
Court of Appeals  
for the Ninth Circuit.

---

ESTATE OF HARRY J. WOLF, Deceased, by  
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with the will annexed of said estate,  
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Transcript of Record

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Petition to Review a Decision of the Tax Court  
of the United States





## INDEX

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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## NAMES AND ADDRESSES OF ATTORNEYS

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Special Attorneys,

Bureau of Internal Revenue.

The Tax Court of the United States

T. C. Docket No. 14,209

HARRY J. WOLF,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

## PETITION

The above-named petitioner hereby petitions the above entitled court for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his Notice of Deficiency, (Bureau Symbols IT:90D:DLA) dated March 3, 1947, and as a basis of his proceeding alleges as follows:

## I.

The petitioner is an individual residing at 3111 S. E. Lambert Street, Portland, Oregon. The returns for the periods here involved were filed with the Collector for District of Oregon. Petitioner made and executed said returns as H. J. Wolf and said Notice of Deficiency was addressed to him as H. J. Wolf for the reason he ordinarily uses only his initials in the transaction of business.

## II.

The Notice of Deficiency (a copy of which is attached and marked Exhibit A) was mailed to the



petitioner from Seattle, Washington, under date of March 3, 1947.

### III.

The taxes in controversy are income taxes for the calendar years 1942 and 1943 and in the amount of \$151,049.05.

### IV.

The determination of the tax set forth in said Notice of Deficiency is based upon the following errors:

(a) The Commissioner erred in refusing to recognize that Jennie Wolf was a partner in the Alaska Junk Company during the Calendar years 1942 and 1943 with an interest therein equal to that of the petitioner.

(b) The Commissioner erred in including an additional \$54,030.87 in petitioner's income for the calendar year 1942 as a result of his refusal to recognize Jennie Wolf as a partner in The Alaska Junk Company.

(c) The Commissioner erred in disallowing as a deduction of the Alaska Junk Company in the calendar year 1943, the sum of \$202,350.60 as (1) a bad debt owed to the Alaska Junk Company by the Oregon Electric Steel Rolling Mills which became worthless in said calendar year, or (2) a loss deductible under the provisions of Sec. 23 (e), I.R.C.

(d) The Commissioner erred in including an additional \$157,689.24 in petitioner's Income Tax

Net Income and in his Victory Tax Net Income for the calendar year 1943 as a result of his refusal to recognize the said Jennie Wolf as a partner in the Alaska Junk Company and his said disallowance of the said sum of \$202,350.60 as a deduction of the Alaska Junk Company. (The refusal to recognize the said partnership interest of Jennie Wolf having the effect of increasing petitioners said income for said calendar year by the sum of \$56,513.94, and his disallowance of the said deduction having the affect of increasing his said income of said calendar year by the sum of \$101,175.30.)

## V.

The facts upon which the petitioner relies as the basis of this proceeding are as follows:

### Re Partnership

(a) At and during the calendar years 1942 and 1943, and for a great many years prior thereto, the petitioner, Jennie Wolf, Sam Schnitzer and Rose Schnitzer were co-partners under the names and styles of The Alaska Junk Company and Schnitzer-Wolf Machinery Company, and as such co-partners were engaged in the business of buying, selling and generally dealing in junk, new and second hand pipe, tools, machinery, hardware, metal and metal products of every character, and in the business activities hereinafter mentioned, and the principal place of business of said partners was in Portland, Oregon. During all said times each of the said per-

sons owned a one-quarter interest in the business and property of said partnership.

(b) The Commissioner refused to recognize that Jennie Wolf and Rose Schnitzer were partners in the said business in the calendar years 1942 and 1943 although he had recognized them as such partners for many years prior thereto, and their interests and shares in said partnership were exactly the same in the calendar years 1942 and 1943 as their interests and shares therein throughout all the years in which the Commissioner did recognize and treat them as partners in said partnership.

(c) Petitioner and Jennie Wolf were intermarried June 16, 1907, and were husband and wife at all times from said date until the death of Jennie Wolf April 8, 1945.

(d) When the petitioner was married he was 23 years of age, had only been in the United States about two years, could speak very little English, was virtually a stranger in Portland, Oregon, and possessed very little information about American business practices. His wife, Jennie Wolf, was educated in Portland, Oregon, and at the time of her marriage to the petitioner she had acquired a good deal of information about business establishments in Portland, Oregon, and about the business of buying and selling second hand goods.

(e) At the time of his said marriage petitioner had in a neighborhood of \$500 or \$600. His wife,

Jennie Wolf, had received \$500 as a wedding present from her father. Immediately after their marriage the petitioner and his wife entered into the business of buying and selling junk and second hand merchandise. Petitioner contributed his said \$500 or \$600 to the capital of said business, and his wife contributed thereto the said sum of \$500, which she had received from her father. The Petitioner and his wife continued in said business from June, 1907, until late in 1911 during which period petitioner's said wife performed valuable services in and to the business mentioned in this paragraph, which services, among other things, consisted of the said Jennie Wolf laying out routes for the petitioner to canvas with a horse and wagon purchased with the said funds, taking part in the management and control of the business, causing a phone to be installed for the use of the business, and in conducting transactions for the said business over the said phone.

(f) Sometime late in the year 1911 petitioner and Sam Schnitzer engaged in a joint adventure in purchasing and disposing of some salvage material being removed from the Portland Hotel. This joint adventure lead to the formation of The Alaska Junk Company.

(g) February 3, 1912, the petitioner, Sam Schnitzer and one Sam Horwitz caused the Alaska Junk Company, to be organized as a corporation under the laws of the State of Oregon with a capital stock of \$5000.00, divided into five shares of a



par value of \$1000 each, and petitioner transferred to said corporation a stock of junk and second hand merchandise of a reasonable value of \$1000.00 in payment for one share of capital stock of said corporation, and Sam Schnitzer transferred junk and second hand merchandise of an equal reasonable value for one share of said capital stock. Sam Horwitz subscribed for but did not completely pay for one share of the capital stock in said corporation. The petitioner and Sam Schnitzer, each paying equal amounts, purchased the interest of Sam Horwitz in said share of capital stock for which he had subscribed.

(h) On April 12, 1912, said corporation was duly dissolved pursuant to a resolution adopted on March 26, 1912, by its board of directors, and its assets were taken over by petitioner and Sam Schnitzer, with equal interests therein, and thereupon they entered into an oral partnership agreement pursuant to which they became partners, with equal interests, under the name and style of The Alaska Junk Company, for the purpose of engaging in the business of buying, selling and generally dealing in junk, pipe and new and second hand tools, hardware, metal and metal goods of every character.

(i) The merchandise transferred by petitioner to said corporation for his share of the said capital stock was purchased by him with the capital and earnings of said business to which Jennie Wolf contributed her money and services as aforesaid, and



the money which the petitioner contributed for said purchase of the interest of Sam Horwitz in the capital stock of said corporation came out of the capital and earnings of said business and/or from earnings of said corporation which Jennie Wolf had assisted in accumulating.

(j) When the partnership last mentioned was organized petitioner and Sam Schnitzer each entered into an agreement with their respective wives whereby the interest of each said wife in said partnership was recognized and fixed as being equal to that of her husband, and whereby it was agreed that each said wife should continue to aid and assist in accumulating money to be retained in the business as capital.

(k) The said partnership business was continuously carried on pursuant to the agreements set forth in paragraph V (h) and V (j) until January 3, 1928, when it was decided by the petitioner, Jennie Wolf, Sam Schnitzer and Rose Schnitzer that they would enter into a formal written partnership agreement, and on the date last mentioned said persons did enter into such an agreement whereby it is provided that the interest of each of the said persons in said partnership should be an equal undivided one-quarter interest and that each of them should be entitled to share equally in the profits and losses of the business, and that the partners should be allowed to draw wages for their services out of the partnership business, which wages should

be considered as a business expense, and that after deducting all business expenses, including wages paid to petitioner and said Sam Schnitzer, the net profits, if any, should be divided into four equal portions and paid to each of the said co-partners, and the losses, if any, should likewise be borne equally.

(l) That said written partnership agreement remained in force and effect from the date it was executed, as aforesaid, to and including the calendar years 1942 and 1943.

(m) Although said written partnership agreement was not executed until said 3rd day of January, 1928, all of the said parties thereto on many occasions from 1912 to the date of said partnership articles reaffirmed their original agreements mentioned in paragraph V (j), and pursuant to said original agreements said wives continued to assist the petitioner and Sam Schnitzer in accumulating money to be retained in the said business as capital; and at all times from the beginning of said partnership in April, 1912, to and including the calendar years 1942 and 1943 Jennie Wolf counseled with and assisted the petitioner in dealing with the problems and affairs of said partnership.

(n) During the calendar years 1942 and 1943 and for many years prior thereto petitioner and Sam Schnitzer drew salaries from said partnership and the same were deducted as business expenses of the partnership prior to any division of the remain-

ing profits by the partners, and said salaries were in compensation to petitioner and Sam Schnitzer for their personal services rendered to the said partnership.

### Re Bad Debt Loss

(o) At and during all the times hereinafter mentioned the Oregon Electric Steel Rolling Mills, hereinafter called the corporation, was a corporation having an authorized capital stock of 2500 shares consisting of common stock of a par value of \$100.00 each, and the petitioner and Sam Schnitzer each subscribed to a portion of the capital stock, which portion was subsequently issued and thereupon immediately reissued so as to divide it equally among petitioner, Jennie Wolf, Sam Schnitzer and Rose Schnitzer. Thereafter additional stock was issued in substantially equal amounts to each of the four persons last mentioned. Said corporation was fully paid for all said stock. The balance of the issued stock of said corporation was owned by other persons, Morris Schnitzer, son of Sam Schnitzer and Rose Schnitzer, owned all of the said balance except three shares.

(p) The said partnership composed of petitioner, Jennie Wolf, Sam Schnitzer and Rose Schnitzer is hereinafter referred to as The Alaska Junk Company. Said Morris Schnitzer at and during all times hereinafter mentioned was engaged in Portland, Oregon, in the business of buying and

selling new and used iron, steel, tools and machinery and conducted such business under the name and style of the Schnitzer Steel Products Co.

(q) In addition to the business activities mentioned in paragraph V (a) The Alaska Junk Company during 1942 and 1943 and for many years prior thereto was engaged in the business of promoting and financing business enterprises of a nature related to the activities of said partnership enumerated in said paragraph V (a).

(r) In the course of its business The Alaska Junk Company between October 22, 1941, and November 22, 1943, on an open account, at the instance and request of said corporation, advanced money to said corporation, either directly or by making payments on its account to its creditors, purchased and furnished it with merchandise charging the cost thereof to it, and sold goods, wares and merchandise to it at the regular prices charged by The Alaska Junk Company to the trade in general. On November 26, 1943, the balance due and owing to The Alaska Junk Company from said corporation on said open account was \$428,132.13.

(s) In consideration of said open account being credited with the sum of \$174,000.00 the said corporation made, executed and delivered to The Alaska Junk Company one hundred seventy-four (174) First Debentures (unsecured) in the total amount of \$174,000.00, bearing interest at 8% per annum, and on July 14, 1943, said Alaska Junk Company



credited said open account with said amount of \$174,000.00, and charged its "Stocks and Bonds" account with a like sum. For a valuable consideration seventy-five (75) such debentures in the sum of \$75,000.00 were also executed and delivered by said corporation to Morris Schnitzer. No payments of either principal or interest were ever made on any of said debentures.

(t) Soon after the organization of said corporation, The Alaska Junk Company and Morris Schnitzer entered into a contract of guaranty whereby it was agreed that in the event a loss should be sustained by The Alaska Junk Company as a result of its extending credit to said corporation, Morris Schnitzer would pay to The Alaska Junk Company so much of any such loss as should exceed two-thirds of the total combined losses of himself and The Alaska Junk Company sustained on account of the extension of credit to said corporation by himself and The Alaska Junk Company, and a corresponding guaranty was made by The Alaska Junk Company to Morris Schnitzer to the extent of one-third of the total combined losses of said parties sustained through the extension of credit to said corporation.

(u) The idea for the establishment of said corporation was conceived by Morris Schnitzer and from its inception to July 17, 1943, he acted as its president and manager. On said date he was inducted into the armed services of the United States



and this left the corporation without a directing head sufficiently informed and capable of carrying out the purposes of the corporation. Extended and repeated efforts were made to secure a suitable manager to take his place. None could be found. None of the remaining stockholders of said corporation or partners of The Alaska Junk Company were able to properly manage the plant. Its operation bogged down. There was a \$678,843.70 mortgage against its real estate. It owed \$149,650.00 for which its inventories were security, and in addition to the sums it owed The Alaska Junk Company and Morris Schnitzer, it owed \$190,684.06 on open accounts. It lost money, became unable to pay its debts, and it became apparent that it would be impossible for it to carry on and operate profitably. Thereupon many industrialists of large financial ability were solicited in repeated efforts to find some person or organization that would take over the interests of The Alaska Junk Company and Morris Schnitzer in said corporation under such terms as would save them from loss, or at least, under terms that would result in as little loss to them as possible. Including those solicited were Kenneth B. Hall and A. M. Mears, then of the Hesse-Ersted Iron Works. After extended negotiations an agreement was made by and between said Hall, Mears, The Alaska Junk Company, and Morris Schnitzer, by his attorney-in-fact Sam Schnitzer, whereby said Hall and Mears agreed to purchase the outstanding stock of said corporation

at a nominal sum and thereafter to cause said corporation to execute and deliver a promissory note to the petitioner, Jennie Wolf, Sam Schnitzer, Rose Schnitzer and Morris Schnitzer in the sum of \$249,000.00 to be secured by a second mortgage upon its properties in payment of all said debentures, and to execute and deliver a promissory note to said persons in the sum of \$151,000.00 secured by a third mortgage upon said properties in compromise and full payment of the balance due on said open account and in complete satisfaction of a debt of \$26,493.77 then due and owing from said corporation to Morris Schnitzer. The Alaska Junk Company entered into said agreement for the reason that it gave The Alaska Junk Company the best opportunity it could find to realize the greatest possible amount on the obligations owed to it by said corporation.

(v) As evidence of the correct balance due The Alaska Junk Company on its said open account a demand promissory note in the amount of said balance was executed and delivered by said corporation to The Alaska Junk Company, and as evidence of the correct amount of said debt owed by said corporation to Morris Schnitzer a demand promissory note in the amount of said debt was executed and delivered by said corporation to Sam Schnitzer, the attorney-in-fact for Morris Schnitzer.

(w) On November 26, 1943, subsequent to the execution and delivery of the demand notes mentioned in paragraph V (v), all of the issued stock

of said corporation was sold to said Hall and Mears and transferred to them or their order pursuant to the agreement mentioned in paragraph V (u); and thereafter said corporation executed and delivered promissory notes and a second and a third mortgage, and the same were accepted by The Alaska Junk Company and Morris Schnitzer, by his said attorney-in-fact, all in accordance with said agreement.

(x) Upon the receipt of said promissory note and second mortgage for the amount of \$249,000.00 all of the said debentures were returned to the said corporation as fully paid and satisfied, and The Alaska Junk Company credited its said open account with \$142,200.33, which was its pro-rata share of the said promissory note and third mortgage for \$151,000.00, and pursuant to said guaranty agreement charged Morris Schnitzer with \$83,581.20 and credited said open account with an equal amount, thereby reducing the balance of said open account to \$202,350.60, which balance became worthless within the calendar year 1943, because under the terms of the settlement with said corporation embodied in the agreement mentioned in paragraph V (u) no further amount could be realized on said unpaid balance from the corporation, and the said sum of \$83,581.20 was the entire amount for which Morris Schnitzer was liable under the said guaranty. On December 31, 1943, The Alaska Junk Company charged off the said balance as a bad debt, and nothing has since been received thereon.

(y) On account of the matters and things hereinabove stated The Alaska Junk Company sustained a bad debt or business loss in the calendar year 1943 in the sum of \$202,350.60.

(z) The Commissioner arbitrarily considered that the said unpaid and worthless balance of \$202,350.60 represented a contribution by The Alaska Junk Company to the capital of said corporation. There was no intention at any time by the petitioner, or any of the other partners, that the said amount, or any portion thereof, should be a capital contribution to said corporation, but on the contrary it was the intention of The Alaska Junk Company that it was extending credit and that the full balance shown by its said open account would be repaid to it by said corporation.

Wherefore, the petitioner prays that this Court may hear this proceeding and determine that the petitioner has paid his tax in full for the calendar years in question and that there is no deficiency in income tax and/or victory tax due from the petitioner for the said years, and prays for such further relief as may be necessary and proper in the premises.

/s/ ROBT. T. JACOB,

Counsel for Petitioner.

State of Oregon,

County of Multnomah—ss.

Harry J. Wolf, being first duly sworn, says that he is the petitioner above named, that he has had



the said petition read to him, and is familiar with the statements contained therein, and that the statements contained therein are true.

/s/ HARRY J. WOLF.

Subscribed and sworn to before me this 24th day of May, 1947.

[Seal]      /s/ J. F. JOHNSON,  
Notary Public for Oregon.

My commission expires March 28, 1951.

Received and filed May 26, 1947.

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EXHIBIT A

Treasury Department  
Internal Revenue Service  
Seattle 1, Washington

March 3, 1947

Office of Internal Revenue Agent in Charge, Seattle  
Division, 305A 1331 Third Avenue Building

IT:90D:DLA

Mr. H. J. Wolf  
3111 S.E. Lambert  
Portland, Oregon

Dear Mr. Wolf:

You are advised that the determination of your income tax liability for the taxable year ended December 31, 1943 discloses a deficiency of \$151,-049.05 as shown in the statement attached.



In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days (not counting Saturday, Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with The Tax Court of the United States, at its principal address, Washington 25, D. C., for a redetermination of the deficiency or deficiencies.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, Seattle 1, Washington for the attention of IT:90D:DLA. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency or deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

JOSEPH D. NUNAN, JR.,

Commissioner,

By /s/ S. R. STOCKTON,

Internal Revenue Agent

in Charge.

DLA:mts

Enclosures:

Statement

Form of waiver

## Statement

IT:90D:DLA

Mr. H. J. Wolf  
3111 S. E. Lambert  
Portland, Oregon

Tax liability for the taxable year ended December 31, 1943.

	Deficiency
Income Tax .....	\$151,049.05

In making this determination of your income tax liability, careful consideration has been given to the report of examination dated June 3, 1946, to your protest dated October 23, 1946 and to the statements made at the conference held on January 22, 1947.

A copy of this letter and statement has been mailed to your representative, Robert T. Jacob, in accordance with the authority contained in the power of attorney executed by you.

## Taxable Year Ended December 31, 1942

## Adjustments to Net Income

Net income as disclosed by return .....	\$ 59,354.01
Unallowable deductions and additional income:	
(a) Income from partnership .....	54,030.87
Total .....	\$113,384.88
Nontaxable income and additional deductions:	
(b) Contributions .....	723.04
Net income adjusted .....	\$112,661.84

## Explanation of Adjustments

(a) It has been determined from an examination of the 1942 return filed by the partnership, Alaska Junk Co., that your distributive share of the income of that partnership was \$118,061.73. Reported on the return, \$64,030.86. Additional income from partnership, \$54,030.87.

(b) It has been determined that your share of contributions made by the partnership, Alaska Junk Co., is \$1,446.08. Deducted on the return, \$723.04. Additional deduction allowed \$723.04.

Mr. H. J. Wolf

Statement

## Computation of Tax

Net income, adjusted .....	\$112,661.84
Less: Personal exemption .....	1,200.00
Surtax net income .....	\$111,461.84
Less: Earned income credit .....	1,400.00
Balance subject to normal tax .....	\$110,061.84
Normal tax at 6 percent on \$110,061.84 \$	6,603.71
Surtax on \$111,461.84 .....	68,194.85
Total tax .....	\$ 74,798.56

## Taxable Year Ended December 31, 1943

## Adjustments to Net Income

	Income Tax Net Income	Victory Tax Net Income
Net income as disclosed by return .....	\$ 61,772.85	\$ 66,968.51
Unallowable deductions and additional income:		
(a) Income from partnership .....	157,689.24	157,689.24
Total .....	\$219,462.09	\$224,657.75
Nontaxable income and additional deductions:		
(b) Contributions .....	981.09	
Net income adjusted .....	\$218,481.00	\$224,657.75

## Explanation of Adjustments

(a) It has been determined from an examination of the 1943 return filed by the partnership, Alaska Junk Co., that your distributive share of the income of that partnership was \$224,203.16. Reported on the return \$66,513.92. Additional income from partnership, \$157,689.24.

(b) It has been determined that your share of contributions made by the partnership, Alaska Junk Co., is \$1,962.18. Deducted on the return, \$981.09. Additional deduction allowed, \$981.09.

Mr. H. J. Wolf

Statement

## Computation of Income and Victory Tax

Income tax net income, adjusted .....	\$218,481.00
Less: Personal exemption .....	1,200.00
Surtax net income .....	\$217,281.00
Less: Earned income credit .....	1,400.00
Balance subject to normal tax .....	\$215,881.00
Normal tax at 6 percent on \$215,881.00..\$	12,952.86
Surtax on \$217,281.00 .....	153,310.42
Total income tax .....	\$166,263.28
Victory tax net income adjusted .....	\$224,657.75
Less: Specific Exemption .....	624.00
Income subject to victory tax .....	\$224,033.75
Victory tax before credit, 5% of \$224,033.75 .....	\$ 11,201.69
Less: Victory tax credit .....	500.00
Net victory tax .....	10,701.69
Net income tax and victory tax .....	\$176,964.97
Income tax for 1942 .....	\$ 74,798.56
Amount of net income tax and victory tax .....	176,964.97
Forgiveness feature:	
(a) Amount of Income tax for 1942....\$	74,798.56
(b) Amount forgiven ( $\frac{3}{4}$ of (a) ) ....	56,098.92
(c) Amount unforgiven .....	18,699.64
Total income and victory tax liability .....	\$195,664.61
Income and victory tax liability disclosed by return Account No. 353532 .....	44,615.56
Deficiency in income and victory tax .....	\$151,049.05

Received and filed May 26, 1947, T.C.U.S.

[Title of Tax Court and Cause.]

### ANSWER

Comes Now the Commissioner of Internal Revenue, by his attorney, Charles Oliphant, Acting Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed herein, admits, denies and alleges as follows:

I. Admits the allegations contained in paragraph I of the petition.

II. Admits the allegations contained in paragraph II of the petition.

III. Admits that the taxes in controversy are, in part, income taxes for the calendar years 1942 and 1943, and that the amount of tax so in controversy is, to wit: \$151,049.05. Denies the remaining allegations contained in paragraph III of the petition. Alleges that said amount, to wit: \$151,049.05, consists, in part, of victory tax for the year 1943, and that by reason of the forgiveness feature of section 6 of the Current Tax Payment Act of 1943, he, the Commissioner, has determined a deficiency in income and victory tax only for the year 1943.

IV(a) to (d), inclusive. Denies that he erred in his determination of the deficiency as shown by the notice of deficiency from which petitioner's appeal



is taken. Specifically denies that he erred in the manner and form as alleged in paragraph IV(a) to (d), inclusive, of the petition.

V(a). Denies the allegations contained in paragraph V(a) of the petition.

(b). Admits his refusal to recognize that Jennie Wolf and Rose Schnitzer were partners in said business in the calendar years 1942 and 1943. Denies the remaining allegations in paragraph V(b) of the petition.

(c). Admits that petitioner and Jennie Wolf were intermarried and were husband and wife at all times during the taxable years 1942 and 1943, and until the death of Jennie Wolf on April 8, 1945. For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth or falsity thereof, denies the remaining allegations contained in paragraph V(c) of the petition.

(d) to (i), inclusive. For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth or falsity thereof, denies the allegations contained in paragraph V(d) to (i), inclusive, of the petition.

(j) to (n), inclusive. Denies the allegations contained in paragraph V(j) to (n), inclusive, of the petition.

(o). For lack of sufficient information or knowledge upon the basis of which to form a belief as to

the truth or falsity thereof, denies the allegations contained in paragraph V(o) of the petition.

(p). For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth or falsity thereof, denies the allegations contained in paragraph V(p) of the petition. Specifically denies that Jennie Wolf and Rose Schnitzer were partners in the business known and carried on under the name of the Alaska Junk Company.

(q) to (x), inclusive. For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth or falsity thereof, denies the allegations contained in paragraph V(q) to (x), inclusive, of the petition.

(y). Denies the allegations contained in paragraph V(y) of the petition.

(z). Admits that he, the Commissioner, considered the balance of \$202,350.60 as a capital investment. Denies the remaining allegations contained in paragraph V(z) of the petition.

VI. Denies generally and specifically each and every material allegation contained in the petition, not hereinbefore specifically admitted, qualified, or denied.

Wherefore, it is prayed that the petitioner's ap-

peal be denied and that the Commissioner's determination of deficiency be approved.

/s/ CHARLES OLIPHANT,

JHP

Acting Chief Counsel, Bureau  
of Internal Revenue.

Of Counsel:

B. H. NEBLETT,

Division Counsel,

JOHN H. PIGG,

R. G. HARLESS,

Special Attorneys,

Bureau of Internal Revenue.

Received and filed Aug. 7, 1947, T.C.U.S.

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[Title of Tax Court and Cause.]

MOTION FOR ORDER GRANTING  
PERMISSION TO AMEND PETITION

Comes now the petitioner in the above entitled cause by Robt. T. Jacob, his counsel of record, and moves the Court for an order permitting him to amend his petition by adding to paragraph V of said petition immediately after sub-paragraph (n) of paragraph V a sub-paragraph to be designated (n.1) in form and substance as follows:

(n.1) During the year 1944 the petitioner instituted proceedings in the Tax Court of the United States against the Commissioner of Internal Rev-

enue by filing in said court a petition, docket number 6262 appealing from a purported deficiency in income taxes for the calendar year 1941, in which petition the petitioner, among other things, alleged:

“(a) Petitioner is a member of the partnership of Alaska Junk Company, which said partnership is composed of four individuals, H. J. Wolf, Mrs. J. Wolf, S. Schnitzer and Mrs. R. Schnitzer, each owning a one-fourth interest therein.”

The Commissioner of Internal Revenue filed his answer to said petition in said court and in his answer admitted the above quoted allegation. Docket numbers 6263, 6264 and 6265 were similar proceedings instituted respectively by Jennie Wolf, Sam Schnitzer and Rose Schnitzer, and in the petitions in each of these dockets there was an allegation similar to the one above quoted, and in answer to each said petition the Commissioner admitted said allegation. Thereafter the said proceeding docket number 6262, and the related dockets 6263, 6264 and 6265 were consolidated for trial and tried by the said Tax Court of the United States, and on or about the 23rd day of December, 1946, the said Tax Court of the United States made and entered findings of fact and its opinion, in which findings of fact the said court found:

“The petitioners are husbands and wives and members of a co-partnership, doing business under the firm name and style of Alaska Junk Company at Portland, Oregon. Each petitioner had a one-fourth interest in the firm. They filed individual



income tax returns with the collector of internal revenue for the district of Oregon.

The partnership, Alaska Junk Company, was originally organized by petitioners, H. J. Wolf and S. Schnitzer, in 1911. Its business was the buying and selling of all sorts of salvage metals and materials. The original partnership continued until 1925 or 1926 when the wives of the partners, petitioners Jennie Wolf and Rose Schnitzer, were taken into the firm. That partnership is still in existence except that petitioner Jennie, the wife of H. J. Wolf, died in April 1945."

On or about the 24th day of September, 1946, the said Court entered its decisions in each of the said causes and each of the said decisions, less formal parts, date, seal and signature, is as follows:

"Pursuant to the determination of the Court, as set forth in its Memorandum Findings of Fact and Opinion, entered Sept. 23, 1946, it is

Ordered and Decided: That there is no deficiency in income tax for the calendar year 1941."

That the findings and decision in docket 6262 was a final adjudication in favor of the petitioner and against the Commissioner of Internal Revenue. Petitioner is named in said docket 6262 as H. J. Wolf. The interest of the petitioner, Sam Schnitzer, Rose Schnitzer and Jennie Wolf in said Alaska Junk Company were exactly the same in the calendar years 1942 and 1943 as in the year 1941, and the fact that each of the said persons has said inter-



ests in said partnership during said years has become res judicata and the respondent ought to be and is estopped to deny the same.

/s/ ROBT. T. JACOB,  
Counsel for Petitioner.

Granted June 10, 1948.

/s/ LUTHER A. JOHNSON,  
Judge.

Filed June 10, 1948, T.C.U.S.

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[Title of Tax Court and Cause.]

#### ANSWER TO AMENDMENT TO PETITION

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for answer to the amendment to petition filed by the above-named petitioner admits and denies as follows:

V-(n.1). Admits the allegations contained in subparagraph (n.1) of paragraph V of the petition except that it is denied that the findings and decision in Docket 6262 was a final adjudication in favor of the petitioner and against the Commissioner of Internal Revenue; that the interest of the petitioner, Sam Schnitzer, Rose Schnitzer and Jennie Wolf in said Alaska Junk Company were exactly the same in the calendar years 1942 and 1943 as in the year 1941, and the fact that each of

the said persons has said interests in said partnership during said years has become res judicata and the respondent ought to be and is estopped to deny the same.

/s/ CHARLES OLIPHANT,  
Chief Counsel, Bureau of  
Internal Revenue.

Of Counsel:

B. H. NEBLETT,  
Division Counsel,

JOHN H. PIGG,  
LEONARD A. MARCUSSEN,  
Special Attorneys,  
Bureau of Internal Revenue.

Received and filed July 28, 1948, T.C.U.S.

The Tax Court of the United States  
Washington

Docket No. 14,209

ESTATE OF HARRY J. WOLF, Deceased, by  
MONTE L. WOLF, the Executor of said  
Estate,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

### DECISION

Pursuant to Opinion of the Tax Court promulgated July 14, 1949, the respondent filed a computation on October 6, 1949, and the petitioner, on November 7, 1949, filed an acquiescence in the computation as filed by the respondent. Now, therefore, it is

Ordered and Decided: That there is a deficiency in income and victory tax due from this petitioner for the calendar year 1943 in the amount of \$43,282.

/s/ LUTHER A. JOHNSON,  
Judge.

Entered Nov. 9, 1949.

Served Nov. 10, 1949.

In the United States Court of Appeals  
for the Ninth Circuit

T. C. Docket No. 14,209

ESTATE OF HARRY J. WOLF, Deceased, by  
MONTE L. WOLF, Administrator de bonis  
non with the will annexed of said Estate,  
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

### PETITION FOR REVIEW

Comes now the petitioner, by his attorneys of record, and respectfully shows this Honorable Court:

#### I.

The petitioner is the duly appointed, qualified and acting Administrator de bonis non with the will annexed of the Estate of Harry J. Wolf, deceased. He resides at 3410 S. E. Woodstock Boulevard, Portland, Oregon, and has his place of business at 900 S. W. First Avenue, Portland, Oregon. The return for the period here involved was filed by Harry J. Wolf with the Collector of Internal Revenue for the District of Oregon.

#### II.

The respondent is the duly appointed, qualified and acting Commissioner of Internal Revenue of

the United States and is hereinafter referred to as the "Commissioner."

### III.

The taxes in controversy are income and victory taxes for the calendar year 1943.

### IV.

#### Nature of Controversy

For many years prior to and during the taxable year before the court Sam Schnitzer, Harry J. Wolf, Rose Schnitzer and Jennie Wolf were doing business as co-partners under the name and style of Alaska Junk Company. During the years 1942 and 1943 Alaska Junk Company was engaged in the business of buying, selling and generally dealing in junk, pipe, tools, machinery, hardware, scrap and other metals and, as a part of its regular business, made loans and advances to customers and affiliated enterprises, always treating these loans and advances as "accounts receivable" on its books of account.

Morris Schnitzer, a son of Sam Schnitzer, was engaged in a similar business and in 1941 organized the Oregon Electric Steel Rolling Mills (hereinafter referred to as "Oregon Steel") an Oregon corporation, to manufacture steel products. The company's authorized capital was 2,500 shares having a par value of \$100.00 each, a total capital of \$250,000.00. Upon final distribution of this stock the partners of Alaska Junk Company received 1,249 shares and Morris Schnitzer 625 shares.



From October, 1941, to November, 1943, Alaska Junk Company advanced to Oregon Steel, cash \$327,870.23, paid bills of \$166,340.16 and furnished goods at market prices to the amount of \$347,341.62, making a total of \$841,552.01. All of these items were charged on Alaska Junk Company's books as "accounts receivable" from Oregon Steel. On the books of Oregon Steel these items were entered as "accounts payable." Alaska Junk Company received payments of cash \$114,519.88, received stock of a par value of \$124,900.00 and debenture notes of a face value of \$174,000.00 making total receipts of \$413,419.88, which items were credited to said accounts receivable.

Morris Schnitzer and Alaska Junk Company orally agreed that Morris Schnitzer would bear  $\frac{1}{3}$  of the total loss, if any, that might be sustained by Morris Schnitzer and Alaska Junk Company from advances to Oregon Steel over and above the advances credited to stock subscriptions. Alaska Junk Company in turn agreed to bear  $\frac{2}{3}$  of any such loss.

Alaska Junk Company was induced to make the advances, sell goods on credit and pay the bills of Oregon Steel upon a promise of early repayment, based upon engineering estimates of minimum earnings of \$50,000.00 per month and a production schedule to begin early in 1943.

In June, 1943, Morris Schnitzer was inducted into military service and Oregon Steel was unable to obtain competent management. As a result of this and other difficulties the operations were unsuccessful.

ful, and in November, 1943, ceased. It was then decided by the stockholders to withdraw from the enterprise, and Oregon Steel stock was then sold. Prior to the sale Oregon Steel issued Alaska Junk Company its promissory note for \$427,843.87, the balance of its account receivable, and issued its note of \$26,829.28 to Schnitzer Steel Products Company (Morris Schnitzer). In exchange for these two notes Alaska Junk Company and Morris Schnitzer received a third mortgage note for \$151,000.00. This compromise resulted in a total loss of \$303,625.90 and by reason of the agreement between Morris Schnitzer and Alaska Junk Company, Alaska Junk Company sustained a loss of \$202,350.60, which was charged off as a bad debt.

On the partnership's return for 1943 a deduction of the \$202,350.60 was claimed as a bad debt. It is this amount which the Commissioner has disallowed as a deduction. The Commissioner's contention was upheld by the Tax Court of the United States and petitioner submits that in making its determination the Tax Court was in error.

## V.

The petitioner designates the following points on which he intends to rely on appeal to the United States Court of Appeals for the Ninth Circuit from the decision heretofore entered by the Tax Court of the United States:

1. The Tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the part-

nership in which petitioner's transferror was a partner was not deductible as a bad debt in computing net income subject to taxation.

2. The Tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the partnership in which petitioner's transferror was a partner was not a bad debt.

3. The Tax Court erred in holding that all of the advances, including said sum of \$202,350.60, of the partnership in which petitioner's transferror was a partner were contributions to capital.

4. The Tax Court erred in not finding and holding that all of said sum of \$202,350.60 was a loan made by the partnership in which petitioner's transferror was a partner.

5. The decision entered by the Tax Court herein is not supported by the evidence, is contrary to the evidence and is in disregard of it.

6. The Tax Court erred in determining that there was a deficiency in income and victory taxes for the calendar year 1943 due from the above named petitioner.

Wherefore, the petitioner petitions that the decision of the Tax Court of the United States be reviewed by the United States Court of Appeals for the Ninth Circuit; that a copy of the record on review be prepared in accordance with law and with the rules of said Court and transmitted to the Clerk of said Court for filing and that appropriate action

be taken by said Court to review and correct the decision of the Tax Court which petitioner submits is erroneous.

/s/ ROBERT T. JACOB,  
/s/ RANDALL S. JONES,  
Attorneys for Petitioner.

Received and filed Jan. 4, 1950, T.C.U.S.

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[Title of Court of Appeals and Cause.]

NOTICE OF FILING OF PETITION  
FOR REVIEW

To: Charles Oliphant, Chief Counsel for the Bureau  
of Internal Revenue.

You will please take notice that on the 4th day of January, 1950, the petitioner above named filed with the Clerk of the Tax Court of the United States at Washington, D. C. a Petition for Review by the United States Court of Appeals for the Ninth Circuit of the decision of the Tax Court of the United States heretofore entered in the above entitled proceeding.

A copy of said Petition for Review as filed is attached hereto and served upon you.

/s/ ROBERT T. JACOB,  
/s/ RANDALL S. JONES.

Receipt of copy acknowledged.

Received and Filed Jan. 9, 1950, T.C.U.S.



The Tax Court of the United States  
Washington

[Title of Cause.]

CERTIFICATE

I, Victor S. Mersch, Clerk of The Tax Court of the United States do hereby certify that the foregoing documents, 1 to 12, inclusive, constitute and are all of the original papers and proceedings before The Tax Court of the United States as set forth in the "Designation of Record" except the original exhibits 1-27, incl., 28, 30, 31, 33-36, incl., 65, 66, 72-79, incl.; A-Z, AA-HH, incl., on file in my office as the original record in the proceeding and in which the petitioner in The Tax Court proceeding has initiated an appeal as above numbered and entitled, together with a true copy of the docket entries in said Tax Court proceeding, as the same appear in the official docket book in my office.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia, this 23rd day of January, 1950.

[Seal]      /s/ VICTOR S. MERSCH,  
Clerk.



[Endorsed]: No. 12472. United States Court of Appeals for the Ninth Circuit. Estate of Harry J. Wolf, Deceased, by Monte L. Wolf, Administrator, de bonis non with the will annexed of said estate, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Petition to Review a Decision of The Tax Court of the United States.

Filed February 7, 1950.

/s/ PAUL P. O'BRIEN,  
Clerk of the United States Court of Appeals for  
the Ninth Circuit.

In the United States Court of Appeals  
for the Ninth Circuit

T. C. Docket No. 14208

SAM SCHNITZER,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

T. C. Docket No. 14209

ESTATE OF HARRY J. WOLF, Deceased, by  
MONTE L. WOLF, Administrator de bonis  
non with the will annexed of said Estate,  
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

T. C. Docket No. 14278

MONTE L. WOLF,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

T. C. Docket No. 14279

BLOSSOM M. GOLDSTEIN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14280

CHARLOTTE C. COHON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14372

ESTATE OF JENNIE WOLF, Deceased, by  
MONTE L. WOLF, Administrator de bonis  
non with the will annexed of said Estate,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

## MOTION TO CONSOLIDATE APPEALS

The above named petitioners on review and each of them, acting by and through their attorneys of record, hereby move this court to consolidate the above entitled proceedings for purposes of the printed record on appeal, the briefing, the hearing,

the argument, the decision and for all other purposes connected with the final disposition of said proceedings on review.

This motion is based on the grounds that all of the above entitled proceedings were consolidated for trial below in the Tax Court, that the Tax Court made but one set of findings of fact and rendered but one opinion in connection with all of these cases, that each of these cases involves the same facts, that each of the petitioners on review was either a partner or is now the transferee of a decedent who was a partner in a partnership known as the Alaska Junk Company, that the sole question for decision concerns the deductibility of a bad debt by said Alaska Junk Company, and that the decision on this single point is determinative of the income tax liability of each of said partners or said transferees of partners who are the petitioners herein.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,

917 Public Service Building,  
Portland 4, Oregon.

I, Randall S. Jones, being on oath first duly sworn, depose and say:

That on the 13th day of February, 1950, I served the foregoing Motion to Consolidate Appeals upon Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, by on said day depositing a duly certified copy thereof in the United

States mails with full postage and registration charges prepaid, addressed to Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, Internal Revenue Building, Washington, D. C. Said papers were deposited in the United States mails at the Federal Post Office, S. W. Sixth and Main Streets, Portland 4, Oregon.

/s/ RANDALL S. JONES.

Subscribed and sworn to before me this 13th day of February, 1950.

[Seal]      /s/ JACQUELINE MOHLAND,  
Notary Public for Oregon.

My commission expires: 9-22-52.

So Ordered:

/s/ WILLIAM DENMAN,  
Chief Judge.

/s/ HOMER BONE,

/s/ WM. E. ORR,  
U. S. Circuit Judge.

[Endorsed]: Filed Feb. 15, 1950.



[Title of Court of Appeals and Causes.]

STATEMENT OF POINTS ON WHICH  
PETITIONERS INTEND TO RELY

The petitioners on review hereby enumerate the points on which they intend to rely on appeal and which are as follows:

1. The Tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the partnership in which petitioners were partners was not a bad debt and not deductible in computing the net income of said partnership and petitioners' net income subject to taxation for the taxable year 1943.

2. The Tax Court erred in holding that the total, or any amount in excess of \$125,000.00, representing bills paid for, cash advanced to, and goods sold to Oregon Electric Steel Rolling Mills by the partnership in which petitioners or their transferrors were partners, constituted a contribution to the capital of said Oregon Electric Steel Rolling Mills.

3. The Tax Court erred in not finding and holding that all and every part of said sum of \$202,350.60 was a debt owed to the partnership in which petitioners were partners.

4. The decision entered by the Tax Court herein is contrary to the law, the Tax Court's findings of fact, and the evidence; and is not supported by said findings of fact or the evidence and is in disregard of both said findings of fact and the evidence.

5. The Tax Court erred in failing to include in its findings material facts clearly established by the evidence which further show that the bills paid, cash advanced and goods sold to Oregon Electric Steel Rolling Mills constituted an indebtedness owed to the partnership.

6. The Tax Court erred in admitting respondent's exhibits O, P, Q, U, V, AA, FF, GG and HH over objections of petitioner for the reasons set forth respectively on pages 120, 121, 122, 129, 134, 137, 495, 589-591, 621 and 636, 639 and 640 of the *Report's* Transcript of the Proceedings before said court.

7. The Tax Court erred in receiving oral testimony adduced by respondent over objections of the petitioners as set forth in those portions from the Reporter's Transcript of the Proceedings before said court which the petitioners have designated for inclusion in the Printed Record.

8. The Tax Court erred in sustaining objections of the respondent to questions asked by petitioners and to oral testimony offered by petitioners, which questions, objections and rulings thereon are set forth in those portions from the Reporter's Transcript of the Proceedings before said court which

the petitioners have designated for inclusion in the Printed Record.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,  
917 Public Service Bldg.,  
Portland 4, Oregon.

I, Randall S. Jones, being on oath first duly sworn, depose and say:

That on the 13th day of February, 1950, I served the Statement of Points on which Petitioners Intend to Rely upon Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, by on said day depositing a duly certified copy thereof in the United States mails with full postage and registration charges prepaid, addressed to Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, Internal Revenue Building, Washington, D. C. Said papers were deposited in the United States mails at the Federal Post Office, S. W. Sixth and Main Streets, Portland 4, Oregon.

/s/ RANDALL S. JONES.

Subscribed and sworn to before me this 13th day of February, 1950.

[Seal] /s/ JACQUELINE MOHLAND,  
Notary Public for Oregon.

My commission expires: 9-22-52.

[Endorsed]: Filed Feb. 15, 1950.



No. 12473

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United States  
Court of Appeals  
For the Ninth Circuit.

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MONTE L. WOLF,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

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Transcript of Record

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Petition to Review a Decision of the Tax Court  
of the United States

FILED

APR 5 1950

PAUL P. O'BRIEN,  
CLERK





No. 12473

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United States  
Court of Appeals  
For the Ninth Circuit.

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MONTE L. WOLF,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

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Transcript of Record

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Petition to Review a Decision of the Tax Court  
of the United States



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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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## NAMES AND ADDRESSES OF ATTORNEYS

ROBT. T. JACOB, ESQ.,

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917 Public Service Bldg.,

Portland 4, Oregon,

Attorneys for Petitioner.

CHARLES OLIPHANT,

Acting Chief Counsel,

Bureau of Internal Revenue,

B. H. NEBLETT,

Division Counsel,

JOHN H. PIGG,

R. G. HARLESS,

Special Attorneys,

Bureau of Internal Revenue.

## The Tax Court of the United States

T. C. Docket No. 14,278

MONTE L. WOLF,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

## PETITION

The above named petitioner hereby petitions the above entitled court for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his Notice of Deficiency, (symbols IT:90D:DLA) dated March 4, 1947, and as a basis of his proceeding alleges as follows:

## I.

The petitioner, an individual, residing at 3410 S. E. Woodstock Boulevard, Portland, Oregon, is one of three equal transferees of the residuary estate of Jennie Wolf, deceased. The returns for the periods here involved were filed by Jennie Wolf with the Collector for District of Oregon.

## II.

The Notice of Deficiency (a copy of which is attached and marked Exhibit A) was mailed to the petitioner from Seattle, Washington, under date of March 4, 1947.

## III.

The taxes in controversy are income taxes for the calendar years 1942 and 1943, and the amount in controversy does not exceed \$42,273.99, which sum is equal to the amount of deficiency asserted. The petitioner contends that at all times during the calendar years 1942 and 1943, Jennie Wolf was a partner in The Alaska Junk Company with an interest therein equal to that of her husband, Harry J. Wolf. Said partnership interest of Jennie Wolf is in issue before this Court in the appeal herein-after mentioned, and in the event this Court in said appeal should determine that Jennie Wolf was not such partner during said calendar years, the petitioner claims that he is entitled to a refund of \$12,316.99 which is one-third of the amount of \$36,950.97 paid by said Jennie Wolf within three years of the mailing of said Notice of Deficiency as income and victory taxes on account of her distributive share of the net income of said partnership for the calendar years of 1942 and 1943.

## IV.

The determination of the tax set forth in said Notice of Deficiency is based upon the following errors:

(a) The Commissioner erred in disallowing as a deduction of The Alaska Junk Company in the calendar year 1943 the sum of \$202,350.60 as (1) a bad debt owed to The Alaska Junk Company by the Oregon Electric Steel Rolling Mills which be-

came worthless in said calendar year, or (2) as a loss deductible under the provisions of Sec. 23 (e), I.R.C.

(b) The Commissioner erred in including an additional \$50,587.65 in the Income Tax Net Income and Victory Tax Net Income of said Jennie Wolf for the calendar year 1943 as a result of his said disallowance of the said sum of \$202,350.60 as a deduction of The Alaska Junk Company for said calendar year.

#### V.

The facts upon which the petitioner relies as the basis of this proceeding are as follows:

#### Re Bad Debt Loss

(a) At and during the calendar years 1942 and 1943, and for a great many years prior thereto, Sam Schnitzer, Rose Schnitzer, Harry J. Wolf and Jennie Wolf were co-partners under the names and styles of The Alaska Junk Company and Schnitzer-Wolf Machinery Company, and as such co-partners were engaged in the business of buying, selling and generally dealing in junk, new and second hand pipe, tools, machinery, hardware, metal and metal products of every character, and in promoting and financing business enterprises of a nature related to the other said activities of said partnership, and the principal place of business of said partners was in Portland, Oregon. During all said times each of the said persons owned a one-quarter interest in the business and property of said partnership, which

said partnership is hereinafter referred to as The Alaska Junk Company.

(b) At and during all the times hereinafter mentioned the Oregon Electric Steel Rolling Mills, hereinafter called the corporation, was a corporation having an authorized capital stock of 2500 shares consisting of common stock of a par value of \$100.00 each. Sam Schnitzer and Harry J. Wolf each subscribed to a portion of the capital stock, which portion was subsequently issued and thereupon immediately reissued so as to divide it equally among said four partners. Thereafter additional stock was issued in substantially equal amounts to each of the four partners. Said corporation was fully paid for all said stock. The balance of the issued stock of said corporation was owned by other persons, Morris Schnitzer, son of Sam Schnitzer and Rose Schnitzer, owned all of the said balance except three shares.

(c) Said Morris Schnitzer at and during all times hereinafter mentioned was engaged in Portland, Oregon, in the business of buying and selling new and used iron, steel, tools and machinery and conducted such business under the name and style of the Schnitzer Steel Products Co.

(d) In the course of its business The Alaska Junk Company between October 22, 1941, and November 22, 1943, on an open account, at the instance and request of said corporation, advanced money to said corporation, either directly or by making payments on its account to its creditors,



purchased and furnished it with merchandise charging the cost thereof to it, and sold goods, wares and merchandise to it at the regular prices charged by The Alaska Junk Company to the trade in general. On November 26, 1943, the balance due and owing to The Alaska Junk Company from said corporation on said open account was \$428,132.13.

(e) In consideration of said open account being credited with the sum of \$174,000.00 the said corporation made, executed and delivered to The Alaska Junk Company one hundred seventy-four (174) First Debentures (unsecured) in the total amount of \$174,000.00, bearing interest at 8% per annum, and on July 14, 1943, said Alaska Junk Company credited said open account with said amount of \$174,000.00, and charged its "Stocks and Bonds" account with a like sum. For a valuable consideration seventy-five (75) such debentures in the sum of \$75,000.00 were also executed and delivered by said corporation to Morris Schnitzer. No payments of either principal or interest were ever made on any of said debentures.

(f) Soon after the organization of said corporation, The Alaska Junk Company and Morris Schnitzer entered into a contract of guaranty whereby it was agreed that in the event a loss should be sustained by The Alaska Junk Company as a result of its extending credit to said corporation, Morris Schnitzer would pay to the Alaska Junk Company so much of any such loss as should exceed two-thirds of the total combined losses of

himself and The Alaska Junk Company sustained on account of the extension of credit to said corporation by himself and The Alaska Junk Company, and a corresponding guaranty was made by The Alaska Junk Company to Morris Schnitzer to the extent of one-third of the total combined losses of said parties sustained through the extension of credit to said corporation.

(g) The idea for the establishment of said corporation was conceived by Morris Schnitzer and from its inception to July 17, 1943, he acted as its president and manager. On said date he was inducted into the armed service of the United States and this left the corporation without a directing head sufficiently informed and capable of carrying out the purposes of the corporation. Extended and repeated efforts were made to secure a suitable manager to take his place. None could be found. None of the remaining stockholders of said corporation or partners of The Alaska Junk Company were able to properly manage the plant. Its operation bogged down. There was a \$678,843.70 mortgage against its real estate. It owed \$149,650.00 for which its inventories were security, and in addition to the sums it owed The Alaska Junk Company and Morris Schnitzer, it owed \$190,684.06 on open accounts. It lost money, became unable to pay its debts, and it became apparent that it would be impossible for it to carry on and operate profitably. Thereupon many industrialists of large financial ability were solicited in repeated efforts to find

some person or organization that would take over the interests of The Alaska Junk Company and Morris Schnitzer in said corporation under such terms as would save them from loss, or at least, under terms that would result in as little loss to them as possible. Including those solicited were Kenneth E. Hall and A. M. Mears, then of the Hesse-Ersted Iron Works. After extended negotiations an agreement was made by and between said Hall, Mears, The Alaska Junk Company, and Morris Schnitzer, by his attorney-in-fact, Sam Schnitzer, whereby said Hall and Mears agreed to purchase the outstanding stock of said corporation at a nominal sum and thereafter to cause said corporation to execute and deliver a promissory note to The Alaska Junk Company and Morris Schnitzer in the sum of \$249,000.00 to be secured by a second mortgage upon its properties in payment of all said debentures, and to execute and deliver a promissory note to said persons in the sum of \$151,000.00 secured by a third mortgage upon said properties in compromise and full payment of the balance due on said open account and in complete satisfaction of a debt of \$26,493.77 then due and owing from said corporation to Morris Schnitzer. The Alaska Junk Company entered into said agreement for the reason that it gave The Alaska Junk Company the best opportunity it could find to realize the greatest possible amount on the obligations owed to it by said corporation.

(h) As evidence of the correct balance due The

Alaska Junk Company on its said open account a demand promissory note in the amount of said balance was executed and delivered by said corporation to The Alaska Junk Company, and as evidence of the correct amount of said debt owed by said corporation to Morris Schnitzer a demand promissory note in the amount of said debt was executed and delivered by said corporation to Sam Schnitzer, the attorney-in-fact for Morris Schnitzer.

(i) On November 26, 1943, subsequent to the execution and delivery of the demand notes mentioned in paragraph V (h), all of the issued stock of said corporation was sold to said Hall and Mears and transferred to them or their order pursuant to the agreement mentioned in paragraph V (g); and thereafter said corporation executed and delivered promissory notes and a second and a third mortgage, and the same were accepted by The Alaska Junk Company and Morris Schnitzer, by his said attorney-in-fact, all in accordance with said agreement.

(j) Upon the receipt of said promissory note and second mortgage for the amount of \$249,000.00 all of the said debentures were returned to the said corporation as fully paid and satisfied, and The Alaska Junk Company credited its said open account with \$142,200.33, which was its pro rata share of the said promissory note and third mortgage for \$151,000.00, and pursuant to said guaranty agreement charged Morris Schnitzer with \$83,581.20 and credited said open account with an equal



amount, thereby reducing the balance of said open account to \$202,350.60, which balance became worthless within the calendar year 1943, because under the terms of the settlement with said corporation embodied in the agreement mentioned in paragraph V (g) no further amount could be realized on said unpaid balance from the corporation, and the said sum of \$83,581.20 was the entire amount for which Morris Schnitzer was liable under the said guaranty. On December 31, 1943, The Alaska Junk Company charged off the said balance as a bed debt, and nothing has since been received thereon.

(k) On account of the matters and things hereinabove stated The Alaska Junk Company sustained a bad debt or business loss in the calendar year 1943 in the sum of \$202,350.60.

(1) The Commissioner arbitrarily considered that the said unpaid and worthless balance of \$202,350.60 represented a contribution by The Alaska Junk Company to the capital of said corporation. Petitioner is informed, believes and therefore alleges that there was no intention at any time by any of the said partners that the said amount, or any portion thereof, should be a capital contribution to said corporation, but on the contrary it was the intention of The Alaska Junk Company that it was extending credit and that the full balance shown by its said open account would be repaid to it by said corporation.



## Re Refund

(m) Said Jennie Wolf was the wife of said Harry J. Wolf and the mother of the petitioner, Charlotte C. Cohon and Blossom M. Goldstein. Jennie Wolf died on April 8, 1945, and left a will which was duly admitted to probate by an order of the Circuit Court of the State of Oregon for the County of Multnomah, Probate Department, made and entered on April 18, 1945, in the Matter of Estate of Jennie Wolf, Deceased, Probate No. 53,-880. By the terms of said will said Jennie Wolf directed that her funeral expenses, just debts, estate and inheritance taxes be paid, bequeathed specific articles of jewelry, household furniture, fixtures, linens, silverware, and certain specified sums of money, and then disposed of all the rest, residue and remainder of her property and estate pursuant to the eighth paragraph of said will. The second and eighth paragraphs of said will read as follows:

“Second: I have a husband named Harry J. Wolf. I have three living children, whose names and the date of their births are as follows, to wit: (1) Monte L. Wolf, who was born on April 5, 1909; and (2) Charlotte C. Cohon—nee Wolf, who was born on September 8, 1911; and (3) Blossom M. Goldstein—nee Wolf, who was born on July 8, 1919.”

“Eighth: I give and bequeath and devise all of the rest, residue and remainder of my property and estate—real and personal and mixed, and wheresoever situated and whether acquired before

or after making this Will—in equal shares to my above named three children.”

There was no person named in said will as a child of Jennie Wolf other than those named in said second paragraph, and she had no other children.

(n) Said Harry J. Wolf, was duly appointed the executor of said will and estate, qualified as such, and administered the estate. He filed his final account, which was duly approved and distribution was ordered by said Court on March 29, 1946. Distribution was thereupon made of all the property and estate of said Jennie Wolf, deceased, that remained in the hands of said executor, and by order of said Court duly made, entered and effective on April 1, 1946, the administration of said estate was fully and completely closed and Harry J. Wolf was discharged and released as executor of said estate. There has been no executor of said will or estate or personal representative of said Jennie Wolf, Deceased, since the date last mentioned; and petitioner is informed, believes and therefor alleges that under the law and practice of the State of Oregon said Harry J. Wolf, by virtue of the order last mentioned, was on said date completely and forever divested of any and all right, power or authority to in any way further act for or on behalf of the said estate which was at the same time fully and completely closed as aforesaid.

(o) The petitioner is informed, believes and therefor alleges that in determining the taxable income of said Harry J. Wolf for the calendar years

1942 and 1943 the Commissioner refused to recognize that Jennie Wolf was a partner during said calendar years in the said business carried on under the name of The Alaska Junk Company with an interest therein equal to that of Harry J. Wolf, although the Commissioner had recognized her as such a partner for many years prior thereto, and that based on his said refusal to recognize her as such partner during said years he treated her distributive share of the net profits of said partnership for said years as income of Harry J. Wolf and determined a deficiency in the income tax liability of said Harry J. Wolf for said calendar years in the sum of \$151,049.05, and that said Harry J. Wolf has filed with the Clerk of this Court, or at least, has mailed to him for filing, an appeal to this Court wherein said Harry J. Wolf alleged that Jennie Wolf was a partner, with such interest, during said calendar years and that the Commissioner erred in refusing to recognize her as such.

(p) In the event the issue referred to in paragraph V (o) should be determined by this Court adversely to said contentions of said Harry J. Wolf, the said Jennie Wolf will have overpaid her income and victory taxes for said calendar years by the sum of \$36,950.97.

(q) All of the specific and pecuniary bequests made by said Jennie Wolf in her said will were paid in full, and the entire amount of said sum of \$36,950.97 was paid on said income and victory taxes in diminution of the interests of petitioner, said

Charlotte C. Cohon and Blossom M. Goldstein as the residuary legatees under said will of said Jennie Wolf, deceased; and in the event of such an adverse determination on said partnership issue, petitioner as a transferee of said Jennie Wolf would be entitled to a refund of one-third of the resultant overpayment as his portion thereof, to wit: he would be entitled to a refund of \$12,316.99.

(r) None of the foregoing allegations are in any way intended as an admission that the Commissioner was correct in his refusal to recognize said partnership interest of Jennie Wolf, and paragraphs (m) through (q) are included herein only to protect the petitioner's interests as a claimant in the event this Court should determine said partnership issue in said appeal adversely to the interests of Harry J. Wolf.

Wherefore, petitioner prays that this Court may hear this proceeding and determine that Jennie Wolf paid her taxes in full for all years in question and that there is no deficiency in her income and/or victory taxes due from petitioner for said years, and petitioner further prays that this cause not be determined by this Court prior to its determination of said partnership issue in said appeal of Harry J. Wolf, and if said issue is determined adversely to the interests of said Harry J. Wolf, then and in such event, that this Court determine that Jennie Wolf made an overpayment of her income and victory taxes for the calendar years in question in the sum of \$36,950.97, and that



she paid the same within three years prior to the mailing of said Notice of Deficiency, and that the petitioner's share in such overpayment, if an overpayment is determined, is \$12,316.99, together with interest thereon as provided by law, and petitioner also prays for such further relief as may be just and proper in the premises.

/s/ ROBT. T. JACOB,

Counsel for Petitioner.

State of Oregon,

County of Multnomah—ss.

Monte L. Wolf, being first duly sworn, says that he is the petitioner above named, that he has read the foregoing petition and is familiar with the statements contained therein, and that the statements contained therein are true, except those stated to be upon information and belief, and those he believes to be true.

/s/ MONTE L. WOLF.

Subscribed and sworn to before me this 26th day of May, 1947.

[Seal] /s/ J. F. JOHNSON,

Notary Public for Oregon.

My Commission expires: March 28, 1951.



## Exhibit A

Treasury Department  
Internal Revenue Service  
Seattle 1, Washington

March 4, 1947.

Office of Internal Revenue Agent in Charge, Seattle Division, 305A 1331 Third Avenue Building.

IT:90D:DLA

Mr. Monte L. Wolf  
3410 S. E. Woodstock Blvd.  
Portland, Oregon

Dear Mr. Wolf:

You are advised that the determination of the income tax liability of the Estate of Jennie Wolf, deceased, 900 S. W. First Avenue, Portland, Oregon, for the taxable year ended December 31, 1943, discloses a deficiency of \$42,273.99, as shown in the statement attached. The amount of the deficiency stated, plus interests as provided by law, constituting your liability as transferee of assets of said Estate of Jennie Wolf, deceased, will be assessed against you.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days (not counting Saturday, Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this

letter, you may file a petition with The Tax Court of the United States, at its principal address, Washington 25, D. C., for a redetermination of the deficiency or deficiencies.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, Seattle 1, Washington for the attention of IT:90D:DLA. The signing and filing of this form will expedite the closing of the return(s) by permitting an early assessment of the deficiency or deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

JOSEPH D. NUNAN, JR.,  
Commissioner.

By /s/ S. R. STOCKTON,  
Internal Revenue Agent in  
Charge.

DLA:mts

Enclosures:

Statement

Form of waiver

IT:90D:DLA

Monte L. Wolf, Transferee

## Statement

Estate of Jennie Wolf, Deceased, Transferor

900 S. W. First Avenue

Portland, Oregon

Tax liability for the taxable year ended December 31, 1943

Monte L. Wolf, Transferee

3410 S. E. Woodstock Blvd.

Portland, Oregon

	Deficiency
Income tax .....	\$ 42,273.99

The records of this office indicate that assets of the above-named decedent's estate were transferred to you on or about April 1, 1946.

The above-stated amount represents your liability as a transferee of assets of the Estate of Jennie Wolf, deceased, 900 S. W. First Avenue, Portland, Oregon, for a deficiency in income tax due from the Estate of Jennie Wolf, deceased, for the taxable year ended December 31, 1943.

## Taxable Year Ended December 31, 1943

## Adjustments to Net Income

	Income Tax Net Income	Victory Tax Net Income
Net income as disclosed by return .....	\$ 52,654.75	\$ 56,514.91
Unallowable deductions and additional income:		
(a) Income from partnership .....	50,587.65	50,587.65
Net income adjusted .....	\$103,242.40	\$107,102.56

## Explanation of Adjustments

(a) It is held after examination of the 1943 return filed by the partnership, Alaska Junk Co., that the distributive share of Jennie Wolf, deceased, of the income from that partnership was \$107,101.58. Reported on the return, \$56,513.93. Additional income from partnership, \$50,587.65.

## Computation of Income and Victory Tax

Income tax net income, adjusted .....	\$103,242.40
Less: Personal exemption .....	None
<b>Surtax net income .....</b>	<b>\$103,242.40</b>
Less: Earned income credit .....	300.00
<b>Balance subject to normal tax .....</b>	<b>\$102,942.40</b>
Normal tax at 6% on \$102,942.40 .....	\$ 6,176.54
Surtax on \$103,242.40 .....	61,701.50
<b>Total income tax .....</b>	<b>\$ 67,878.04</b>
Victory tax net income adjusted .....	\$107,102.56
Less: Specific exemption .....	624.00
<b>Income subject to victory tax .....</b>	<b>\$106,478.56</b>
Victory tax before credit, 5% of \$106,478.56 .....	\$ 5,323.93
Less: Victory tax credit .....	500.00
<b>Net victory tax .....</b>	<b>4,823.93</b>
<b>Net income tax and victory tax .....</b>	<b>\$ 72,701.97</b>
<b>Income tax for 1942 .....</b>	<b>\$ 26,091.94</b>
<b>Amount of net income tax and victory tax .....</b>	<b>\$ 72,701.97</b>
Forgiveness feature:	
(a) Amount of income tax for 1942....	\$ 26,091.94
(b) Amount forgiven ( $\frac{3}{4}$ of (a) ).....	19,568.95
(c) Amount unforgiven .....	6,522.99
<b>Total income and victory tax liability.....</b>	<b>\$ 79,224.96</b>
Income and victory tax liability disclosed by return	
Account No. 353534 .....	36,950.97
<b>Deficiency of income tax .....</b>	<b>\$ 42,273.99</b>

Received and filed May 29, 1947, T.C.U.S.

[Title of Tax Court and Cause.]

### ANSWER

Comes Now the Commissioner of Internal Revenue, by his attorney, Charles Oliphant, Acting Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed herein, admits, denies and alleges as follows:

I. Admits the allegations contained in paragraph I of the petition.

II. Admits the allegations contained in paragraph II of the petition.

III. Admits that the taxes in controversy are, in part, income taxes for the calendar years 1942 and 1943; that the amount of the taxes so in controversy, exclusive of interest as provided by law, is, to wit: \$42,273.99, and that the alleged partnership interest of the decedent, Jennie Wolf, in the business known and carried on under the name of Alaska Junk Company during the years 1942 and 1943 is in controversy before this Court. Denies the remaining allegations contained in paragraph III of the petition, but admits that petitioner makes the contentions as set forth in said paragraph. Alleges that said amount of, to wit: \$42,273.99, consists, in part, of victory tax for the year 1943; that the income tax liability of the decedent, Jennie Wolf, for the year 1942, is involved in this proceeding only by reason of the forgiveness feature of section 6 of the Current Tax Payment Act of 1943; that no part of the defi-



ciency in income and victory tax as determined by respondent to be due from petitioner's transferor, the Estate of Jennie Wolf, Deceased, for the taxable year 1943, in the amount of, to wit: \$42,273.99, arises out of or is attributable to any adjustment made by respondent to or in respect of the net income as reported by petitioner's said transferor and/or said transferor's decedent, Jennie Wolf, for the taxable year 1942, and that the alleged partnership interest of the decedent, Jennie Wolf, in the business known and carried on under the name of Alaska Junk Company during the years 1942 and 1943 is in issue before this Court in the related proceedings entitled Harry J. Wolf, Docket No. 14209, and Sam Schnitzer, Docket No. 14278; also, in the related transferee proceedings entitled Blossom M. Goldstein, Docket No. 14279, and Charlotte C. Cohon, Docket No. 14280.

IV (a) and (b). Denies that he erred in his determination of the deficiency shown by the notice of deficiency from which petitioner's appeal is taken. Specifically denies that he erred in the manner and form as alleged in paragraph IV (a) and (b) of the petition.

V (a). Denies the allegations contained in paragraph V (a) of the petition, except to the extent that in the event the decisions of this Court in the pending related cases of Harry J. Wolf, Docket No. 14209, and Sam Schnitzer, Docket No. 14208, should be adverse to respondent, i.e., the Court's decisions in those cases should be predicated upon his find-

ing and holding by said Court that the decedent, Jennie Wolf, was, during the taxable years 1942 and 1943, a valid and bona fide partner in the business known and carried on under the name of Alaska Junk Company, and said decisions shall have become final, then and in that event, and upon that condition only, the respondent admits the allegations contained in said paragraph V (a) of the petition.

(b) to (j), inclusive. For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth or falsity thereof, denies the allegations contained in paragraph V (b) to (j), inclusive, of the petition.

(k) Denies the allegations contained in paragraph V(k) of the petition.

(l). Admits that he, the Commissioner, considered the balance of \$202,350.60 as a capital investment. Denies the remaining allegations contained in paragraph V(1) of the petition.

(m). Admits the allegations contained in paragraph V(m) of the petition.

(n). Admits the allegations contained in paragraph V(n) of the petition, except that it is denied that said Harry J. Wolf is now divested of any right, power or authority to act for and on behalf of said estate.

(o). Admits that he, the Commissioner, in determining the taxable income of said Harry J. Wolf, for the calendar years 1942 and 1943, refused to recognize that Jennie Wolf was a part-

ner during said calendar years in the business carried on under the name of Alaska Junk Company with an interest therein equal to that of Harry J. Wolf; that based on his said refusal to recognize the decedent, Jennie Wolf, as such partner during said years, he treated her alleged distributive share of net profits of said business for said years as income of Harry J. Wolf and determined a deficiency in the income and victory tax liability of said Harry J. Wolf for the year 1943 in the amount of, to wit: \$151,049.05; and that said Harry J. Wolf has filed with this Court his petition, at Docket No. 14209, as aforesaid, wherein he alleged that the decedent, Jennie Wolf, was a partner, with such interest, during said years, and that the Commissioner erred in refusing to recognize her as such. Denies the remaining allegations contained in paragraph V(o) of the petition.

(p). Admits that in the event the issue referred to in paragraph V(o) of the petition, which said issue is presented in the pending proceeding entitled Harry J. Wolf, Docket No. 14209, as aforesaid, should be determined by this Court adversely to the contentions of said Harry J. Wolf, the decedent, the said Jennie Wolf, will have overpaid her income and victory tax for the year 1943. For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth or falsity thereof, denies the remaining allegations contained in paragraph V(p) of the petition.

(q). Admits that all of the specific and pecu-

niary bequests made by said Jennie Wolf in her said will were paid in full. Denies the remaining allegations contained in paragraph V(q) of the petition.

(r). Because of the absence of any allegation of fact therein, respondent neither admits nor denies the statements set forth in paragraph V(r) of the petition.

VI. Denies generally and specifically each and every material allegation contained in the petition, not hereinbefore specifically admitted, qualified, or denied.

VII. For further answer to the petition herein, respondent alleges as follows:

(a). That the taxpayer, namely: Jennie Wolf, now deceased, and formerly of Portland, Oregon, from whom respondent determined the deficiency involved in this proceeding to be due, died on, to wit: April 8, 1945, a resident of the State of Oregon; that said decedent died testate; that said decedent's will was duly admitted to probate by order of the Circuit Court of the State of Oregon for the County of Multnomah, Probate Department, made and entered April 18, 1945.

(b). That by the terms of said will, said decedent directed payment of all expenses and debts, made specific bequests and then disposed of all the rest, residue and remainder of her property and estate, pursuant to paragraph eight (8) of said will. The second and eighth paragraphs of said will read as follows:



“Second: I have a husband named Harry J. Wolf; I have three living children, whose names and the date of their births are as follows, to wit: 1) Monte L. Wolf, who was born on April 5, 1909; and (2) Charlotte C. Cohon—nee Wolf, who was born on September 8, 1911; and (3) Blossom L. Goldstein—nee Wolf, who was born on July 8, 1919.

\* \* \*

“Eighth: I give and bequeath and devise all of the rest, residue and remainder of my property and estate—real and personal and mixed, and wheresoever situated and whether acquired before or after making this Will—in equal shares to my above named three children.”

(c). That the petitioner herein is one of the three children mentioned in paragraph eight (8) of said will as a residuary legatee.

(d). That a final account by the duly appointed and authorized executor of the Estate of Jennie Wolf, Deceased, was filed with the said court on March 29, 1946, and was duly approved, and distribution was ordered by said court on March 29, 1946.

(e). That pursuant to the order of said court above referred to, distribution was thereupon made of all the property and estate of said Jennie Wolf, Deceased, that remained in the hands of said executor and by order of said court duly made, entered and effective on April 1, 1946, the administration of said estate was fully and completely closed



and said executor was discharged and released as executor of said estate.

(f). That the distribution in accord with the terms of the will of said decedent, and pursuant to said order of said court, has the effect of rendering the Estate of Jennie Wolf, Deceased, insolvent.

(g). That the deficiency in income tax involved in this proceeding for the taxable year 1943, in the amount of \$42,273.99, has not been paid, and that the same is now due and owing to the United States, together with interest thereon, as provided by law.

(h). That at the time of her death, testate, on, to wit: April 8, 1945, as aforesaid, the decedent, Jennie Wolf, was the owner of property and assets of the then fair market value in excess of the deficiency in income tax involved in this proceeding, together with interest thereon as provided by law.

(i). That by reason of paragraph eight (8) of the said will of decedent, as aforesaid, the petitioner herein was one of the three legatees of the decedent and distributees of the assets of the estate of said decedent; that as such legatee and distributee, there were distributed to the petitioner, on or about April 1, 1946, assets and property of the decedent and of the decedent's estate of a then fair market value in excess of the amount of the deficiency and/or tax liability involved in this proceeding, together with interest thereon as provided by law.

(j). That by reason of the premises, the peti-

itioner herein became and is now liable as a transferee of the property of the taxpayer, Jennie Wolf, Deceased, and has become and is now answerable to the extent of the amount of said deficiency in income tax, together with interest thereon as provided by law.

Wherefore, it is prayed that petitioner's appeal be denied; that the respondent's determination be approved; and that the petitioner herein be held to be liable at law or in equity as a transferee of the assets of the taxpayer, Jennie Wolf, Deceased.

/s/ CHARLES OLIPHANT, JHP  
Acting Chief Counsel, Bureau  
of Internal Revenue.

Of Counsel:

B. H. NEBLETT,  
Division Counsel.

JOHN H. PIGG,  
R. G. HARLESS,  
Special Attorneys,  
Bureau of Internal Revenue.

Received and Filed Aug. 7, 1947.

[Title of Tax Court and Cause.]

## REPLY

The above-named petitioner, for reply to the allegations affirmatively set out by the respondent in his answer, admits, denies and alleges as follows:

VII(a). Admits the allegations contained in paragraph VII(a) of the answer, except the petitioner denies that the deficiency involved in this proceeding is or was due from Jennie Wolf, Deceased.

(b) and (c). Admits the allegations contained in paragraph VII(b) and VII(c) of the answer.

(d). Denies that the final account mentioned in paragraph VII(d) of the answer was filed on March 29, 1946. Alleges it was filed on February 27, 1946. Admits all the remaining allegations mentioned in said paragraph.

(e). Admits the allegations contained in paragraph VII(e) of the answer.

(f). Admits that the distribution mentioned in paragraph VII(f) of the answer was had in accord with the terms of the will of Jennie Wolf, Deceased, and pursuant to the order referred to in said paragraph, and that said distribution left the Estate of Jennie Wolf, Deceased, without assets. Denies all the remaining allegations contained in said paragraph of the answer.

(g). Admits that the deficiency in income tax involved in this proceeding for the taxable year 1943, in the amount of \$42,273.99, has not been paid. Denies all the remaining allegations contained in

paragraph VII(g) of the answer, and particularly denies that the amount of \$42,273.99 or interest thereon, or any other amount or interest thereon is now due and owing to the United States on account of the matters or taxes in controversy in this proceeding.

(h). Admits the allegations contained in paragraph VII(h) of the answer, except petitioner denies that any deficiency or interest thereon in the income tax involved in this proceeding is due or owing to the United States.

(i). Admits that by reason of paragraph eight (8) of the will of the decedent, Jennie Wolf, the petitioner herein was one of the three legatees of said decedent and distributees of the assets of the estate of said decedent; that as such legatee and distributee, there were distributed to the petitioner, on or about April 1, 1946, assets and property of the decedent and of decedent's estate. Denies all the remaining allegations contained in paragraph VII(i) of the answer, except as in this paragraph next alleged. Alleges that the fair market value as of April 1, 1946, and the appraised value of the said assets and property so distributed to petitioner was in the sum of \$26,534.44 and did not exceed said sum.

(j). Denies the allegations contained in paragraph VII(j) of the answer, and particularly denies that the petitioner is liable as a transferee of the property of the taxpayer, Jennie Wolf, Deceased, and has become or is now answerable to the extent of the amount of the alleged deficiency

in income tax, together with interest thereon or in or to any other amount or interest thereon.

VIII. Denies generally and specifically each and every material allegation contained in paragraphs VII(a) to (j), inclusive, of respondent's answer, not hereinbefore especially admitted, qualified or denied.

Wherefore, the petitioner prays that the respondent's determination be disapproved, that the prayer in the answer be denied, and that the prayer in the petition be granted.

/s/ ROBT. T. JACOB,

Counsel for Petitioner.

State of Oregon,

County of Multnomah—ss.

Monte L. Wolf, being first duly sworn, says that he is the petitioner above named, that he has read the foregoing reply and is familiar with the statements contained therein, and that the statements contained therein are true, except those stated to be upon information and belief, and those he believes to be true.

/s/ MONTE L. WOLF.

Subscribed and sworn to before me this 10th day of November, 1947.

[Seal] /s/ J. H. JOHNSON,

Notary Public for Oregon.

My Commission expires: 3/28/51.

[Lodged]: Nov. 19, 1947.

Filed Nov. 20, 1947, T.C.U.S.



[Title of Tax Court and Cause.]

MOTION FOR ORDER GRANTING PERMISSION TO AMEND PETITION

Comes now the petitioner in the above entitled cause by Robt. T. Jacob, his counsel of record, and moves the Court for an order permitting him to amend his petition by adding to paragraph V of said petition immediately after sub-paragraph (a) of paragraph V a sub-paragraph to be designated (a.1) in form and substance as follows:

(a.1) During the year 1944 said Jennie Wolf instituted proceedings in the Tax Court of the United States against the Commissioner of Internal Revenue by filing in said court a petition, docket number 6263, appealing from a purported deficiency in income taxes for the calendar year 1941, in which petition said Jennie Wolf, as the petitioner therein, among other things, alleged:

“(a) Petitioner is a member of the partnership of Alaska Junk Company, which said partnership is composed of four individuals, H. J. Wolf, Mrs. J. Wolf, S. Schnitzer and Mrs. R. Schnitzer, each owning a one-fourth interest therein.”

The Commissioner of Internal Revenue filed his answer to said petition in said court and in his answer admitted the above quoted allegation. Docket numbers 6262, 6264 and 6265 were similar proceedings instituted respectively by Harry J. Wolf, Sam Schnitzer and Rose Schnitzer, and in the petitions in each of these dockets there was an allegation

similar to the one above quoted, and in the answer to each said petition the Commissioner admitted said allegation. Thereafter the said proceeding docket number 6263, and the related dockets 6262, 6264 and 6265 were consolidated for trial and tried by the said Tax Court of the United States, and on or about the 23rd day of December, 1946 the said Tax Court of the United States made and entered findings of fact and its opinion, in which findings of fact the said court found:

“The petitioners are husbands and wives and members of a co-partnership, doing business under the firm name and style of Alaska Junk Company at Portland, Oregon. Each petitioner had a one-fourth interest in the firm. They filed individual income tax returns with the collector of internal revenue for the district of Oregon.

The partnership, Alaska Junk Company, was originally organized by petitioners, H. J. Wolf and S. Schnitzer, in 1911. Its business was the buying and selling of all sorts of salvage metals and materials. The original partnership continued until 1925 or 1926 when the wives of the partners, petitioners Jennie Wolf and Rose Schnitzer, were taken into the firm. That partnership is still in existence except that petitioner Jennie Wolf, the wife of H. J. Wolf, died in April 1945.”

On or about the 24th day of September, 1946 the said Court entered its decisions in each of the said causes and each of the said decisions, less formal parts, date, seal and signature, is as follows:

“Pursuant to the determination of the Court, as set forth in its Memorandum Findings of Fact and Opinion, entered Sept. 23, 1946, it is

Ordered and Decided: That there is no deficiency in income tax for the calendar year 1941.”

That the findings and decision in docket 6263 was a final adjudication in favor of said Jennie Wolf and against the Commissioner of Internal Revenue. The interest of Sam Schnitzer, Rose Schnitzer, Harry J. Wolf and Jennie Wolf in said Alaska Junk Company were exactly the same in the calendar years 1942 and 1943 as in the year 1941, and the fact that each of the said persons has said interests in said partnership during said years has become *res judicata* and the Respondent ought to be and is estopped to deny the same.

/s/ ROBT. T. JACOB,  
Counsel for Petitioner.

Granted June 10, 1948.

/s/ LUTHER A. JOHNSON,  
Judge.

Filed June 10, 1948, T.C.U.S.

[Title of Tax Court and Cause.]

ANSWER TO AMENDMENT TO PETITION

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for answer to the amendment to petition filed by the above-named petitioner admits and denies as follows:

V-(a.1). Admits the allegations contained in subparagraph (a.1) of paragraph V of the petition except those contained in the last two sentences thereof which are denied.

/s/ CHARLES OLIPHANT,

Chief Counsel,

Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,

Division Counsel;

JOHN H. PIGG,

LEONARD A. MARCUSSEN,

Special Attorneys,

Bureau of Internal Revenue.

Served July 29, 1948.

Received and filed July 28, 1948, T.C.U.S.

The Tax Court of the United States  
Washington

Docket No. 14278

MONTE L. WOLF,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

DECISION

Pursuant to Opinion of the Tax Court promulgated July 14, 1949, the respondent filed a computation on October 6, 1949, and the petitioner, on November 7, 1949, filed an acquiescence in the computation as filed by the respondent. Now, therefore, it is

Ordered and Decided: That there is a deficiency in income and victory tax due from this petitioner for the calendar year 1943 in the amount of \$42,273.99.

/s/ LUTHER A. JOHNSON,  
Judge.

Entered Nov. 9, 1949.

Served Nov. 10, 1949.



In the United States Court of Appeals  
for the Ninth Circuit

T. C. Docket No. 14278

MONTE L. WOLF,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

### PETITION FOR REVIEW

Comes now the petitioner, by his attorneys of record, and respectfully shows this Honorable Court:

#### I.

The petitioner is an individual residing at 3410 S. E. Woodstock Boulevard, Portland, Oregon, and is one of three equal transferees of the residuary estate of Jennie Wolf, deceased. The return for the period here involved was filed by Jennie Wolf with the Collector of Internal Revenue for the District of Oregon.

#### II.

The respondent is the duly appointed, qualified and acting Commissioner of Internal Revenue of the United States and is hereinafter referred to as the "Commissioner."

#### III.

The taxes in controversy are income and victory taxes for the calendar year 1943.

## IV.

## Nature of Controversy

For many years prior to and during the taxable year before the court Sam Schnitzer, Harry J. Wolf, Rose Schnitzer and Jennie Wolf were doing business as copartners under the name and style of Alaska Junk Company. During the years 1942 and 1943 Alaska Junk Company was engaged in the business of buying, selling and generally dealing in junk, pipe, tools, machinery, hardware, scrap and other metals and, as a part of its regular business, made loans and advances to customers and affiliated enterprises, always treating these loans and advances as "accounts receivable" on its books of account.

Morris Schnitzer, a son of Sam Schnitzer, was engaged in a similar business and in 1941 organized the Oregon Electric Steel Rolling Mills (hereinafter referred to as "Oregon Steel") an Oregon corporation, to manufacture steel products. The company's authorized capital was 2,500 shares having a par value of \$100.00 each, a total capital of \$250,000.00 Upon final distribution of this stock the partners of Alaska Junk Company received 1,249 shares and Morris Schnitzer 625 shares.

From October, 1941 to November, 1943 Alaska Junk Company advanced to Oregon Steel, cash \$327,870.23, paid bills of \$166,340.16 and furnished goods at market prices to the amount of \$347,341.62, making a total of \$841,552.01. All of these items

were charged on Alaska Junk Company's books as "accounts receivable" from Oregon Steel. On the books of Oregon Steel these items were entered as "accounts payable." Alaska Junk Company received payments of cash \$114,519.88, received stock of a par value of \$124,900.00 and debenture notes of a face value of \$174,000.00 making total receipts of 413,419.88, which items were credited to said accounts receivable.

Morris Schnitzer and Alaska Junk Company orally agreed that Morris Schnitzer would bear  $\frac{1}{3}$  of the total loss, if any, that might be sustained by Morris Schnitzer and Alaska Junk Company from advances to Oregon Steel over and above the advances credited to stock subscriptions. Alaska Junk Company in turn agreed to bear  $\frac{2}{3}$  of any such loss.

Alaska Junk Company was induced to make the advances, sell goods on credit and pay the bills of Oregon Steel upon a promise of early repayment, based upon engineering estimates of minimum earnings of \$50,000.00 per month and a production schedule to begin early in 1943.

In June, 1943 Morris Schnitzer was inducted into military service and Oregon Steel was unable to obtain competent management. As a result of this and other difficulties the operations were unsuccessful, and in November, 1943 ceased. It was then decided by the stockholders to withdraw from the enterprise, and Oregon Steel stock was then sold. Prior to the sale Oregon Steel issued Alaska Junk

Company its promissory note for \$427,843.87, the balance of its account receivable, and issued its note of \$26,829.28 to Schnitzer Steel Products Company (Morris Schnitzer). In exchange for these two notes Alaska Junk Company and Morris Schnitzer received a third mortgage note for \$151,000.00. This compromise resulted in a total loss of \$303,625.90 and by reason of the agreement between Morris Schnitzer and Alaska Junk Company, Alaska Junk Company sustained a loss of \$202,350.60, which was charged off as a bad debt.

On the partnership's return for 1943 a deduction of the \$202,350.60 was claimed as a bad debt. It is this amount which the Commissioner has disallowed as a deduction. The Commissioner's contention was upheld by the Tax Court of the United States and petitioner submits that in making its determination the Tax Court was in error.

## V.

The petitioner designates the following points on which he intends to rely on appeal to the United States Court of Appeals for the Ninth Circuit from the decision heretofore entered by the Tax Court of the United States:

1. The Tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the partnership in which petitioner's transferror was a partner was not deductible as a bad debt in computing net income subject to taxation.

2. The Tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the



partnership in which petitioner's transferror was a partner was not a bad debt.

3. The Tax Court erred in holding that all of the advances, including said sum of \$202,350.60, of the partnership in which petitioner's transferror was a partner were contributions to capital.

4. The Tax Court erred in not finding and holding that all of said sum of \$202,350.60 was a loan made by the partnership in which petitioner's transferror was a partner.

5. The decision entered by the Tax Court herein is not supported by the evidence, is contrary to the evidence and is in disregard of it.

6. The Tax Court erred in determining that there was a deficiency in income and victory taxes for the calendar year 1943 due from the above named petitioner.

Wherefore, the petitioner petitions that the decision of the Tax Court of the United States be reviewed by the United States Court of Appeals for the Ninth Circuit; that a copy of the record on review be prepared in accordance with law and with the rules of said Court and transmitted to the Clerk of said Court for filing and that appropriate action be taken by said Court to review and correct the decision of the Tax Court which petitioner submits is erroneous.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,

Attorneys for Petitioner.

Received and filed Jan. 4, 1950, T.C.U.S.



[Title of Court of Appeals and Cause.]

NOTICE OF FILING OF PETITION  
FOR REVIEW

To: Charles Oliphant, Chief Counsel for the Bureau  
of Internal Revenue.

You will please take notice that on the 4th day  
of January, 1950, the petitioner above named filed  
with the Clerk of the Tax Court of the United  
States at Washington, D. C. a Petition for Review  
by the United States Court of Appeals for the  
Ninth Circuit of the decision of the Tax Court of  
the United States heretofore entered in the above  
entitled proceeding.

A copy of said Petition for Review as filed is at-  
tached hereto and served upon you.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES.

Received and filed Jan. 9, 1950, T.C.U.S.

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[Endorsed]: No. 12473. United States Court of  
Appeals for the Ninth Circuit. Monte L. Wolf, Pe-  
titioner, vs. Commissioner of Internal Revenue, Re-  
spondent. Transcript of the Record. Petition to  
Review a Decision of The Tax Court of the United  
States.

Filed February 7, 1950.

/s/ PAUL P. O'BRIEN,

Clerk of the United States Court of Appeals for  
the Ninth Circuit.

The Tax Court of the United States  
Washington

[Title of Cause.]

CERTIFICATE

I, Victor S. Mersch, Clerk of The Tax Court of the United States do hereby certify that the foregoing documents 1 to 13, inclusive, constitute and are all of the original papers and proceedings before The Tax Court of the United States as set forth in the "Designation of Record" except the original exhibits 1-27, incl., 28, 30, 31, 33-36, incl., 65, 66, 72-79, incl.; A-Z, AA-HH, incl., on file in my office as the original record in the proceeding and in which the petitioner in The Tax Court proceeding has initiated an appeal as above numbered and entitled, together with a true copy of the docket entries in said Tax Court proceeding, as the same appear in the official docket book in my office.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia, this 23rd day of January, 1950.

[Seal]      /s/ VICTOR S. MERSCH,  
Clerk.

In the United States Court of Appeals  
for the Ninth Circuit

T. C. Docket No. 14208

SAM SCHNITZER,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

T. C. Docket No. 14209

ESTATE OF HARRY J. WOLF, Deceased, by  
MONTE L. WOLF, Administrator de bonis  
non with the will annexed of said Estate,  
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

T. C. Docket No. 14278

MONTE L. WOLF,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

T. C. Docket No. 14279

BLOSSOM M. GOLDSTEIN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14280

CHARLOTTE C. COHON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14372

ESTATE OF JENNIE WOLF, Deceased, by  
MONTE L. WOLF, Administrator de bonis  
non with the will annexed of said Estate,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

## MOTION TO CONSOLIDATE APPEALS

The above named petitioners on review and each of them, acting by and through their attorneys of record, hereby move this court to consolidate the above entitled proceedings for purposes of the printed record on appeal, the briefing, the hearing,

the argument, the decision and for all other purposes connected with the final disposition of said proceedings on review.

This motion is based on the grounds that all of the above entitled proceedings were consolidated for trial below in the Tax Court, that the Tax Court made but one set of findings of fact and rendered but one opinion in connection with all of these cases, that each of these cases involves the same facts, that each of the petitioners on review was either a partner or is now the transferee of a decedent who was a partner in a partnership known as the Alaska Junk Company, that the sole question for decision concerns the deductibility of a bad debt by said Alaska Junk Company, and that the decision on this single point is determinative of the income tax liability of each of said partners or said transferees of partners who are the petitioners herein.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,

917 Public Service Building,  
Portland 4, Oregon.

I, Randall S. Jones, being on oath first duly sworn, depose and say:

That on the 13th day of February, 1950, I served the foregoing Motion to Consolidate Appeals upon Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, by on said day depositing a duly certified copy thereof in the United



States mails with full postage and registration charges prepaid, addressed to Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, Internal Revenue Building, Washington, D. C. Said papers were deposited in the United States mails at the Federal Post Office, S. W. Sixth and Main Streets, Portland 4, Oregon.

/s/ RANDALL S. JONES.

Subscribed and sworn to before me this 13th day of February, 1950.

[Seal] /s/ JACQUELINE MOHLAND,  
Notary Public for Oregon.

My commission expires: 9-22-52.

So Ordered:

/s/ WILLIAM DENMAN,  
Chief Judge.

/s/ HOMER BONE,

/s/ WM. E. ORR,

U. S. Circuit Judge.

[Endorsed]: Filed Feb. 15, 1950.

[Title of Court of Appeals and Causes.]

STATEMENT OF POINTS ON WHICH  
PETITIONERS INTEND TO RELY

The petitioners on review hereby enumerate the points on which they intend to rely on appeal and which are as follows:

1. The Tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the partnership in which petitioners were partners was not a bad debt and not deductible in computing the net income of said partnership and petitioners' net income subject to taxation for the taxable year 1943.

2. The Tax Court erred in holding that the total, or any amount in excess of \$125,000.00, representing bills paid for, cash advanced to, and goods sold to Oregon Electric Steel Rolling Mills by the partnership in which petitioners or their transferrors were partners, constituted a contribution to the capital of said Oregon Electric Steel Rolling Mills.

3. The Tax Court erred in not finding and holding that all and every part of said sum of \$202,350.60 was a debt owed to the partnership in which petitioners were partners.

4. The decision entered by the Tax Court herein is contrary to the law, the Tax Court's findings of fact, and the evidence; and is not supported by said findings of fact or the evidence and is in disregard of both said findings of fact and the evidence.

5. The Tax Court erred in failing to include in its findings material facts clearly established by the evidence which further show that the bills paid, cash advanced and goods sold to Oregon Electric Steel Rolling Mills constituted an indebtedness owed to the partnership.

6. The Tax Court erred in admitting respondent's exhibits O, P, Q, U, V, AA, FF, GG and HH over objections of petitioner for the reasons set forth respectively on pages 120, 121, 122, 129, 134, 137, 495, 589-591, 621 and 636, 639 and 640 of the *Report's* Transcript of the Proceedings before said court.

7. The Tax Court erred in receiving oral testimony adduced by respondent over objections of the petitioners as set forth in those portions from the Reporter's Transcript of the Proceedings before said court which the petitioners have designated for inclusion in the Printed Record.

8. The Tax Court erred in sustaining objections of the respondent to questions asked by petitioners and to oral testimony offered by petitioners, which questions, objections and rulings thereon are set forth in those portions from the Reporter's Transcript of the Proceedings before said court which

the petitioners have designated for inclusion in the Printed Record.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,

917 Public Service Bldg.,  
Portland 4, Oregon.

I, Randall S. Jones, being on oath first duly sworn, depose and say:

That on the 13th day of February, 1950, I served the Statement of Points on which Petitioners Intend to Rely upon Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, by on said day depositing a duly certified copy thereof in the United States mails with full postage and registration charges prepaid, addressed to Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, Internal Revenue Building, Washington, D. C. Said papers were deposited in the United States mails at the Federal Post Office, S. W. Sixth and Main Streets, Portland 4, Oregon.

/s/ RANDALL S. JONES.

Subscribed and sworn to before me this 13th day of February, 1950.

[Seal] /s/ JACQUELINE MOHLAND,  
Notary Public for Oregon.

My commission expires: 9-22-52.

[Endorsed]: Filed Feb. 15, 1950.





No. 12474

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United States  
Court of Appeals  
for the Ninth Circuit.

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BLOSSOM M. GOLDSTEIN,

Petitioner,

VS.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

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Transcript of Record

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Petition to Review a Decision of the Tax Court  
of the United States

FILED

APR 1 1939

PAUL P. O'BRIEN  
CLERK



No. 12474

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United States  
Court of Appeals  
for the Ninth Circuit.

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BLOSSOM M. GOLDSTEIN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

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Transcript of Record

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Petition to Review a Decision of the Tax Court  
of the United States



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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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## NAMES AND ADDRESSES OF ATTORNEYS

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Acting Chief Counsel,  
Bureau of Internal Revenue,

B. H. NEBLETT,

Division Counsel, .

JOHN H. PIGG,

R. G. HARLESS,

Special Attorneys,  
Bureau of Internal Revenue.

The Tax Court of the United States

T. C. Docket 14279

BLOSSOM M. GOLDSTEIN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

### PETITION

The above-named petitioner hereby petitions the above-entitled Court for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his Notice of Deficiency, (symbols IT: 90D:DLA) dated March 4, 1947, and as a basis of her proceeding alleges as follows:

#### I.

The petitioner, an individual, residing at 3111 S. E. Lambert Street, Portland, Oregon, is one of three equal transferees of the residuary estate of Jennie Wolf, deceased. The returns for the period here involved were filed by Jennie Wolf with the Collector for District of Oregon.

#### II.

The Notice of Deficiency (a copy of which is attached and marked Exhibit A) was mailed to the petitioner from Seattle, Washington, under date of March 4, 1947.

## III.

The taxes in controversy are income taxes for the calendar years 1942 and 1943, and the amount in controversy does not exceed \$42,273.99, which sum is equal to the amount of deficiency asserted. The petitioner contends that at all times during the calendar years 1942 and 1943, Jennie Wolf was a partner in The Alaska Junk Company with an interest therein equal to that of her husband, Harry J. Wolf. Said partnership interest of Jennie Wolf is in issue before this Court in the appeal hereinafter mentioned, and in the event this Court in said appeal should determine that Jennie Wolf was not such partner during said calendar years, the petitioner claims that she is entitled to a refund of \$12,-316.99 which is one-third of the amount of \$36,-950.97 paid by said Jennie Wolf within three years of the mailing of said Notice of Deficiency as income and victory taxes on account of her distributive share of the net income of said partnership for the calendar years of 1942 and 1943.

## IV.

The determination of the tax set forth in said Notice of Deficiency is based upon the following errors:

(a) The Commissioner erred in disallowing as a deduction of The Alaska Junk Company in the calendar year 1943 the sum of \$202,350.60 as (1) a bad debt owed to The Alaska Junk Company by the Oregon Electric Steel Rolling Mills which be-

came worthless in said calendar year, or (2) as a loss deductible under the provisions of Sec. 23 (e), I.R.C.

(b) The Commissioner erred in including an additional \$50,587.65 in the Income Tax Net Income and Victory Tax Net Income of said Jennie Wolf for the calendar year 1943 as a result of his said disallowance of the said sum of \$202,350.60 as a deduction of The Alaska Junk Company for said calendar year.

## V.

The facts upon which the petitioner relies as the basis of this proceeding are as follows:

### Re Bad Debt Loss

(a) At and during the calendar years 1942 and 1943, and for a great many years prior thereto, Sam Schnitzer, Rose Schnitzer, Harry J. Wolf and Jennie Wolf were co-partners under the names and styles of The Alaska Junk Company and Schnitzer-Wolf Machinery Company, and as such co-partners were engaged in the business of buying, selling and generally dealing in junk, new and second hand pipe, tools, machinery, hardware, metal and metal products of every character, and in promoting and financing business enterprises of a nature related to the other said activities of said partnership, and the principal place of business of said partners was in Portland, Oregon. During all said times each of the said persons owned a one-quarter interest in the business and property of



said partnership, which said partnership is hereinafter referred to as The Alaska Junk Company.

(b) At and during all the times hereinafter mentioned the Oregon Electric Steel Rolling Mills, hereinafter called the corporation, was a corporation having an authorized capital stock of 2500 shares consisting of common stock of a par value of \$100.00 each, Sam Schnitzer and Harry J. Wolf each subscribed to a portion of the capital stock, which portion was subsequently issued and thereupon immediately reissued so as to divide it equally among said four partners. Thereafter additional stock was issued in substantially equal amounts to each of the four partners. Said corporation was fully paid for all stock. The balance of the issued stock of said corporation was owned by other persons, Morris Schnitzer, son of Sam Schnitzer and Rose Schnitzer, owned all of the said balance except three shares.

(c) Said Morris Schnitzer at and during all times hereinafter mentioned was engaged in Portland, Oregon, in the business of buying and selling new and used iron, steel, tools and machinery and conducted such business under the name and style of the Schnitzer Steel Products Co.

(d) In the course of its business The Alaska Junk Company between October 22, 1941, and November 22, 1943, on an open account, at the instance and request of said corporation, advanced money to said corporation, either directly or by

making payments on its account to its creditors, purchased and furnished it with merchandise charging the cost thereof to it, and sold goods, wares and merchandise to it at the regular prices charged by The Alaska Junk Company to the trade in general. On November 26, 1943, the balance due and owing to The Alaska Junk Company from said corporation on said open account was \$428,132.13.

(e) In consideration of said open account being credited with the sum of \$174,000.00 the said corporation made, executed and delivered to The Alaska Junk Company one hundred seventy-four (174) First Debentures (unsecured) in the total amount of \$174,000.00, bearing interest at 8% per annum, and on July 14, 1943, said Alaska Junk Company credited said open account with said amount of \$174,000.00, and charged its "Stocks and Bonds" account with a like sum. For a valuable consideration seventy-five (75) such debentures in the sum of \$75,000.00 were also executed and delivered by said corporation to Morris Schnitzer. No payments of either principal or interest were ever made on any of said debentures.

(f) Soon after the organization of said corporation, The Alaska Junk Company and Morris Schnitzer entered into a contract of guaranty whereby it was agreed that in the event a loss should be sustained by The Alaska Junk Company as a result of its extending credit to said corporation, Morris Schnitzer would pay to The Alaska

Junk Company so much of any such loss as should exceed two-thirds of the total combined losses of himself and The Alaska Junk Company sustained on account of the extension of credit to said corporation by himself and The Alaska Junk Company, and a corresponding guaranty was made by The Alaska Junk Company to Morris Schnitzer to the extent of one-third of the total combined losses of said parties sustained through the extension of credit to said corporation.

(g) The idea for the establishment of said corporation was conceived by Morris Schnitzer and from its inception to July 17, 1943, he acted as its president and manager. On said date he was inducted into the armed service of the United States and this left the corporation without a directing head sufficiently informed and capable of carrying out the purposes of the corporation. Extended and repeated efforts were made to secure a suitable manager to take his place. None could be found. None of the remaining stockholders of said corporation or partners of The Alaska Junk Company were able to properly manage the plant. Its operation bogged down. There was a \$678,843.70 mortgage against its real estate. It owed \$149,650.00 for which its inventories were security, and in addition to the sums it owed The Alaska Junk Company and Morris Schnitzer, it owed \$190,684.06 on open accounts. It lost money, became unable to pay its debts, and it became apparent that it would be impossible for it to carry on and operate prof-

itably. Thereupon many industrialists of large financial ability were solicited in repeated efforts to find some person or organization that would take over the interests of The Alaska Junk Company and Morris Schnitzer in said corporation under such terms as would save them from loss, or at least, under terms that would result in as little loss to them as possible. Including those solicited were Kenneth E. Hall and A. M. Mears, then of the Hesse-Ersted Iron Works. After extended negotiations an agreement was made by and between said Hall, Mears, The Alaska Junk Company, and Morris Schnitzer, by his attorney-in-fact, Sam Schnitzer, whereby said Hall and Mears agreed to purchase the outstanding stock of said corporation at a nominal sum and thereafter to cause said corporation to execute and deliver a promissory note to The Alaska Junk Company and Morris Schnitzer in the sum of \$249,000.00 to be secured by a second mortgage upon its properties in payment of all said debentures, and to execute and deliver a promissory note to said persons in the sum of \$151,000.00 secured by a third mortgage upon said properties in compromise and full payment of the balance due on said open account and in complete satisfaction of a debt of \$26,493.77 then due and owing from said corporation to Morris Schnitzer. The Alaska Junk Company entered into said agreement for the reason that it gave The Alaska Junk Company the best opportunity it could find to real-



ize the greatest possible amount on the obligations owed to it by said corporation.

(h) As evidence of the correct balance due The Alaska Junk Company on its said open account a demand promissory note in the amount of said balance was executed and delivered by said corporation to The Alaska Junk Company, and as evidence of the correct amount of said debt owed by said corporation to Morris Schnitzer a demand promissory note in the amount of said debt was executed and delivered by said corporation to Sam Schnitzer, the attorney-in-fact for Morris Schnitzer.

(i) On November 26, 1943, subsequent to the execution and delivery of the demand notes mentioned in paragraph V (h), all of the issued stock of said corporation was sold to said Hall and Mears and transferred to them or their order pursuant to the agreement mentioned in paragraph V (g); and thereafter said corporation executed and delivered promissory notes and a second and a third mortgage, and the same were accepted by The Alaska Junk Company and Morris Schnitzer, by his said attorney-in-fact, all in accordance with said agreement.

(j) Upon the receipt of said promissory note and second mortgage for the amount of \$249,000.00 all of the said debentures were returned to the said corporation as fully paid and satisfied, and The Alaska Junk Company credited its said open account with \$142,200.33, which was its pro-rata share



of the said promissory note and third mortgage for \$151,000.00, and pursuant to said guaranty agreement charged Morris Schnitzer with \$83,581.20 and credited said open account with an equal amount, thereby reducing the balance of said open account to \$202,350.60, which balance became worthless within the calendar year 1943, because under the terms of the settlement with said corporation embodied in the agreement mentioned in paragraph V (g) no further amount could be realized on said unpaid balance from the corporation, and the said sum of \$83,581.20 was the entire amount for which Morris Schnitzer was liable under the said guaranty. On December 31, 1943, The Alaska Junk Company charged off the said balance as a bad debt, and nothing has since been received thereon.

(k) On account of the matters and things hereinabove stated The Alaska Junk Company sustained a bad debt or business loss in the calendar year 1943 in the sum of \$202,350.60.

(1) The Commissioner arbitrarily considered that the said unpaid and worthless balance of \$202,350.60 represented a contribution by The Alaska Junk Company to the capital of said corporation. Petitioner is informed, believes and therefore alleges that there was no intention at any time by any of the said partners that the said amount, or any portion thereof, should be a capital contribution to said corporation, but on the contrary it was the intention of The Alaska Junk Company that it was

extending credit and that the full balance shown by its said open account would be repaid to it by said corporation.

### Re Refund

(m) Said Jennie Wolf was the wife of said Harry J. Wolf and the mother of the petitioner, Charlotte C. Cohon and Monte L. Wolf. Jennie Wolf died on April 8, 1945, and left a will which was duly admitted to probate by an order of the Circuit Court of the State of Oregon for the County of Multnomah, Probate Department, made and entered on April 18, 1945, in the Matter of Estate of Jennie Wolf, Deceased, Probate No. 53880. By the terms of said will said Jennie Wolf directed that her funeral expenses, just debts, estate and inheritance taxes be paid, bequeathed specific articles of jewelry, household furniture, fixtures, linens, silverware, and certain specified sums of money, and then disposed of all the rest, residue and remainder of her property and estate pursuant to the eighth paragraph of said will. The second and eighth paragraphs of said will read as follows:

“Second: I have a husband named Harry J. Wolf, I have three living children, whose names and the date of their births are as follows, to wit: (1) Monte L. Wolf, who was born on April 5, 1909; and (2) Charlotte C. Cohon—nee Wolf, who was born on September 8, 1911; and (3) Blossom M. Goldstein—nee Wolf, who was born on July 8, 1919.”

“Eighth: I give and bequeath and devise all the rest, residue and remainder of my property and estate—real and personal and mixed, and wheresoever situated and whether acquired before or after making this Will—in equal shares to my above-named three children.”

There was no person named in said will as a child of Jennie Wolf other than those named in said second paragraph, and she had no other children.

(n) Said Harry J. Wolf was duly appointed the executor of said will and estate, qualified as such, and administered the estate. He filed his final account, which was duly approved and distribution was ordered by said Court on March 29, 1946. Distribution was thereupon made of all the property and estate of said Jennie Wolf, Deceased, that remained in the hands of said executor, and by order of said Court duly made, entered and effective on April 1, 1946, the administration of said estate was fully and completely closed and Harry J. Wolf was discharged and released as executor of said estate. There has been no executor of said will or estate or personal representative of said Jennie Wolf, Deceased, since the date last mentioned; and petitioner is informed, believes and therefore alleges that under the law and practice of the State of Oregon said Harry J. Wolf, by virtue of the order last mentioned, was on said date completely and forever divested of any and all right, power or authority to in any way further act for

or on behalf of the said estate which was at the same time fully and completely closed as aforesaid.

(o) The petitioner is informed, believes and therefore alleges that in determining the taxable income of said Harry J. Wolf for the calendar years 1942 and 1943 the Commissioner refused to recognize that Jennie Wolf was a partner during said calendar years in the said business carried on under the name of The Alaska Junk Company with an interest therein equal to that of Harry J. Wolf, although the Commissioner had recognized her as such a partner for many years prior thereto, and that based on his said refusal to recognize her as such partner during said years he treated her distributive share of the net profits of said partnership for said years as income of Harry J. Wolf and determined a deficiency in the income tax liability of said Harry J. Wolf for said calendar years in the sum of \$151,049.05, and that said Harry J. Wolf has filed with the Clerk of this Court, or at least, has mailed to him for filing, an appeal to this Court wherein said Harry J. Wolf alleged that Jennie Wolf was a partner, with such interest, during said calendar years and that the Commissioner erred in refusing to recognize her as such.

(p) In the event the issue referred to in paragraph V (o) should be determined by this Court adversely to said contentions of said Harry J. Wolf, the said Jennie Wolf will have overpaid her income and victory taxes for said calendar years by the sum of \$36,950.97.



(q) All of the specific and pecuniary bequests made by said Jennie Wolf in her said will were paid in full, and the entire amount of said sum of \$36,950.97 was paid on said income and victory taxes in diminution of the interests of petitioner, said Charlotte C. Cohon and Monte L. Wolf as the residuary legatees under said will of said Jennie Wolf, Deceased; and in the event of such an adverse determination on said partnership issue, petitioner as a transferee of said Jennie Wolf would be entitled to a refund of one-third of the resultant overpayment as her portion thereof, to wit: she would be entitled to a refund of \$12,316.99.

(r) None of the foregoing allegations are in any way intended as an admission that the Commissioner was correct in his refusal to recognize said partnership interest of Jennie Wolf, and paragraphs (m) through (q) are included herein only to protect the petitioner's interests as a claimant in the event this Court should determine said partnership issue in said appeal adversely to the interests of Harry J. Wolf.

Wherefore, petitioner prays that this Court may hear this proceeding and determine that Jennie Wolf paid her taxes in full for all years in question and that there is no deficiency in her income and/or victory taxes due from petitioner for said years, and petitioner further prays that this cause not be determined by this Court prior to its determination of said partnership issue in said appeal



of Harry J. Wolf, and if said issue is determined adversely to the interests of said Harry J. Wolf, then and in such event, that this Court determine that Jennie Wolf made an overpayment of her income and victory taxes for the calendar years in question in the sum of \$36,950.97, and that she paid the same within three years prior to the mailing of said Notice of Deficiency, and that the petitioner's share in such overpayment, if an overpayment is determined, is \$12,316.99, together with interest thereon as provided by law, and petitioner also prays for such further relief as may be just and proper in the premises.

/s/ ROBERT T. JACOB,  
Counsel for Petitioner.

State of Oregon,  
County of Multnomah—ss.

Blossom M. Goldstein, being first duly sworn, says that she is the petitioner above named, that she has read the foregoing petition, and is familiar with the statements contained therein, and that the statements contained therein are true, except those stated to be upon information and belief, and those she believes to be true.

/s/ BLOSSOM M. GOLDSTEIN.

Subscribed and sworn to before me this 26th day of May, 1947.

[Seal] /s/ J. F. JOHNSON,  
Notary Public for Oregon.

My Commission expires: March 28, 1951.

## Exhibit A

Treasury Department  
Internal Revenue Service  
Seattle 1, Washington

March 4, 1947.

Office of Internal Revenue Agent in Charge Seattle  
Division, 305A 1331 Third Avenue Building

IT:90D:DLA

Mrs. Blossom M. Goldstein  
3111 S. E. Lambert  
Portland, Oregon

Dear Mrs. Goldstein:

You are advised that the determination of the income tax liability of the Estate of Jennie Wolf, deceased, 900 S. W. First Avenue, Portland, Oregon, for the taxable year ended December 31, 1943, discloses a deficiency of \$42,273.99, as shown in the statement attached. The amount of the deficiency stated, plus interest as provided by law, constituting your liability as transferee of assets of said Estate of Jennie Wolf, deceased, will be assessed against you.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days (not counting Saturday, Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this let-

ter, you may file a petition with The Tax Court of the United States, at its principal address, Washington 25, D. C., for a redetermination of the deficiency or deficiencies.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, Seattle 1, Washington, for the attention of IT:90D:DLA. The signing and filing of this form will expedite the closing of the return(s) by permitting an early assessment of the deficiency or deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

JOSEPH D. NUNAN, JR.,

Commissioner.

By /s/ S. R. STOCKTON,

Internal Revenue Agent in  
Charge.

DLA:mts

Enclosures:

Statement

Form of Waiver

IT:90D:DLA

Blossom M. Goldstein, Transferee

## Statement

Estate of Jennie Wolf, Deceased, Transferor  
900 S. W. First Avenue  
Portland, Oregon

Tax liability for the taxable year ended December 31, 1943.

Mrs. Blossom M. Goldstein  
3111 S. E. Lambert  
Portland, Oregon

	Deficiency
Income tax .....	\$ 42,273.99

The records of this office indicate that assets of the above-named decedent's estate were transferred to you on or about April 1, 1946.

The above-stated amount represents your liability as a transferee of assets of the Estate of Jennie Wolf, deceased, 900 S. W. First Avenue, Portland, Oregon, for a deficiency in income tax due from the Estate of Jennie Wolf, deceased, for the taxable year ended December 31, 1943.

## Adjustments to Net Income

	Income Tax Net Income	Victory Tax Net Income
Net income as disclosed by return .....	\$ 52,654.75	\$ 56,514.91
Unallowable deductions and additional income:		
(a) Income from partnership .....	50,587.65	50,587.65
Net income adjusted .....	\$103,242.40	\$107,102.56

## Explanation of Adjustments

(a) It is held after examination of the 1943 return filed by the partnership, Alaska Junk Co., that the distributive share of Jennie Wolf, deceased, of the income from that partnership was \$107,101.58. Reported, on the return, \$56,513.93. Additional income from partnership, \$50,587.65.

## Computation of Income and Victory Tax

Income tax net income adjusted .....	\$103,242.40	
Less: Personal exemption .....	None	
<hr/>		
Surtax net income .....	\$103,242.40	
Less: Earned income credit .....	300.00	
<hr/>		
Balance subject to normal tax .....	\$102,942.40	
<hr/>		
Normal tax at 6% on \$102,942.40 .....	\$ 6,176.54	
Surtax on \$103,242.40 .....	61,701.50	
<hr/>		
Total income tax .....	\$ 67,878.04	
<hr/>		
Victory tax net income adjusted .....	\$107,102.56	
Less: Specific exemption .....	624.00	
<hr/>		
Income subject to victory tax .....	\$106,478.56	
<hr/>		
Victory tax before credit, 5% of		
\$106,478.56 .....	\$ 5,323.93	
Less: Victory tax credit .....	500.00	
<hr/>		
Net victory tax .....	4,823.93	
<hr/>		
Net income tax and victory tax .....	\$ 72,701.97	
<hr/>		
Income tax for 1942 .....	\$ 26,091.94	
<hr/>		
Amount of net income tax and victory tax .....	\$ 72,701.97	
<hr/>		
Forgiveness feature:		
(a) Amount of income tax for 1942....	\$ 26,091.94	
(b) Amount forgiven ( $\frac{3}{4}$ of (a) ) ....	19,568.95	
<hr/>		
(c) Amount unforgiven .....	6,522.99	
<hr/>		
Total income and victory tax liability .....	\$ 79,224.96	
Income and victory tax liability disclosed by return		
Account No. 353534 .....	36,950.97	
<hr/>		
Deficiency of income tax .....	\$ 42,273.99	

Received and filed May 29, 1947, T.C.U.S.



[Title of Tax Court and Cause.]

## ANSWER

Comes now the Commissioner of Internal Revenue, by his attorney, Charles Oliphant, Acting Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed herein, admits, denies and alleges as follows:

I. Admits the allegations contained in paragraph I of the petition.

II. Admits the allegations contained in paragraph II of the petition.

III. Admits that the taxes in controversy are, in part, income taxes for the calendar years 1942 and 1943; that the amount of the taxes so in controversy, exclusive of interest as provided by law, is, to-wit: \$42,273.99, and that the alleged partnership interest of the decedent, Jennie Wolf, in the business known and carried on under the name of Alaska Junk Company during the years 1942 and 1943 is in controversy before this Court. Denies the remaining allegations contained in paragraph III of the petition, but admits that petitioner makes the contentions as set forth in said paragraph. Alleges that said amount of, to wit: \$42,273.99, consists, in part, of victory tax for the year 1943; that the income tax liability of the decedent, Jennie Wolf, for the year 1942, is involved in this proceeding only by reason of the forgiveness feature of section 6 of the Current Tax Payment Act of 1943; that no part

of the deficiency in income and victory tax as determined by respondent to be due from petitioner's transferor, the Estate of Jennie Wolf, Deceased, for the taxable year 1943, in the amount of, to wit: \$42,273.99, arises out of or is attributable to any adjustment made by respondent to or in respect of the net income as reported by petitioner's said transferor and/or said transferor's decedent, Jennie Wolf, for the taxable year 1942, and that the alleged partnership interest of the decedent, Jennie Wolf, in the business known and carried on under the name of Alaska Junk Company during the years 1942 and 1943 is in issue before this Court in the related proceedings entitled Harry J. Wolf, Docket No. 14209, and Sam Schnitzer, Docket No. 14278; also, in the related transferee proceedings entitled Monte L. Wolf, Docket No. 14278, and Charlotte C. Cohon, Docket No. 14280.

IV(a) and (b). Denies that he erred in his determination of the deficiency shown by the notice of deficiency from which petitioner's appeal is taken. Specifically denies that he erred in the manner and form as alleged in paragraph IV(a) and (b) of the petition.

V(a). Denies the allegations contained in paragraph V(a) of the petition, except to the extent that in the event the decisions of this Court in the pending related cases of Harry J. Wolf, Docket No. 14209, and Sam Schnitzer, Docket No. 14208, should be adverse to respondent, i.e., the Court's decisions

in those cases should be predicated upon his finding and holding by said Court that the decedent, Jennie Wolf, was, during the taxable years 1942 and 1943, a valid and bona fide partner in the business known and carried on under the name of Alaska Junk Company, and said decisions shall have become final, then and in that event, and upon that condition only, the respondent admits the allegations contained in said paragraph V(a) of the petition.

(b) to (j), inclusive. For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth or falsity thereof, denies the allegations contained in paragraph V(b) to (j), inclusive, of the petition.

(k). Denies the allegations contained in paragraph V(k) of the petition.

(l). Admits that he, the Commissioner, considered the balance of \$202,350.60 as a capital investment. Denies the remaining allegations contained in paragraph V(1) of the petition.

(m). Admits the allegations contained in paragraph V(m) of the petition.

(n). Admits the allegations contained in paragraph V(n) of the petition, except that it is denied that said Harry J. Wolf is now divested of any right, power or authority to act for and on behalf of said estate.

(o). Admits that he, the Commissioner, in determining the taxable income of said Harry J. Wolf, for the calendar years 1942 and 1943, refused to recognize that Jennie Wolf was a partner during said calendar years in the business carried on under the name of Alaska Junk Company with an interest therein equal to that of Harry J. Wolf; that based on his said refusal to recognize the decedent, Jennie Wolf, as such partner during said years, he treated her alleged distributive share of net profits of said business for said years as income of Harry J. Wolf and determined a deficiency in the income and victory tax liability of said Harry J. Wolf for the year 1943 in the amount of, to wit: \$151,049.05; and that said Harry J. Wolf has filed with this Court his petition, at Docket No. 14209, as aforesaid, wherein he alleged that the decedent, Jennie Wolf, was a partner, with such interest, during said years, and that the Commissioner erred in refusing to recognize her as such. Denies the remaining allegations contained in paragraph V(o) of the petition.

(p). Admits that in the event the issue referred to in paragraph V(o) of the petition, which said issue is presented in the pending proceeding entitled Harry J. Wolf, Docket No. 14209, as aforesaid, should be determined by this Court adversely to the contentions of said Harry J. Wolf, the decedent, the said Jennie Wolf, will have overpaid her income and victory tax for the year 1943. For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth



or falsity thereof, denies the remaining allegations contained in paragraph V(p) of the petition.

(q). Admits that all of the specific and pecuniary bequests made by said Jennie Wolf in her said will were paid in full. Denies the remaining allegations contained in paragraph V(q) of the petition.

(r). Because of the absence of any allegation of fact therein, respondent neither admits nor denies the statements set forth in paragraph V(r) of the petition.

VI. Denies generally and specifically each and every material allegation contained in the petition, not hereinbefore specifically admitted, qualified, or denied.

VII. For further answer to the petition herein, respondent alleges as follows:

(a). That the taxpayer, namely: Jennie Wolf, now deceased, and formerly of Portland, Oregon, from whom respondent determined the deficiency involved in this proceeding to be due, died on, to wit: April 8, 1945, a resident of the State of Oregon; that said decedent died testate; that said decedent's will was duly admitted to probate by order of the Circuit Court of the State of Oregon for the County of Multnomah, Probate Department, made and entered April 18, 1945.

(b). That by the terms of said will, said decedent directed payment of all expenses and debts,



made specific bequests and then disposed of all the rest, residue and remainder of her property and estate, pursuant to paragraph eight (8) of said will. The second and eighth paragraphs of said will read as follows:

“Second: I have a husband named Harry J. Wolf; I have three living children, whose names and the date of their births are as follows, to-wit: (1) Monte L. Wolf, who was born on April 5, 1909; and (2) Charlotte C. Cohon—nee Wolf, who was born on September 8, 1911; and (3) Blossom M. Goldstein—nee Wolf, who was born on July 8, 1919.

\* \* \*

“Eighth: I give and bequeath and devise all of the rest, residue and remainder of my property and estate—real and personal and mixed, and wheresoever situated and whether acquired before or after making this Will—in equal shares to my above named three children.”

(c). That the petitioner herein is one of the three children mentioned in paragraph eight (8) of said will as a residuary legatee.

(d). That a final account by the duly appointed and authorized executor of the Estate of Jennie Wolf, Deceased, was filed with the said court on March 29, 1946, and was duly approved, and distribution was ordered by said court on March 29, 1946.

(e). That pursuant to the order of said court above referred to, distribution was thereupon made

of all the property and estate of said Jennie Wolf, Deceased, that remained in the hands of said executor and by order of said court duly made, entered and effective on April 1, 1946, the administration of said estate was fully and completely closed and said executor was discharged and released as executor of said estate.

(f). That the distribution in accord with the terms of the will of said decedent, and pursuant to said order of said court, had the effect of rendering the Estate of Jennie Wolf, Deceased, insolvent.

(g). That the deficiency in income tax involved in this proceeding for the taxable year 1943, in the amount of \$42,273.99, has not been paid, and that the same is now due and owing to the United States, together with interest thereon, as provided by law.

(h). That at the time of her death, testate, on, to wit: April 8, 1945, as aforesaid, the decedent, Jennie Wolf, was the owner of property and assets of the then fair market value in excess of the deficiency in income tax involved in this proceeding, together with interest thereon as provided by law.

(i). That by reason of paragraph eight (8) of the said will of decedent, as aforesaid, the petitioner herein was one of the three legatees of the decedent and distributees of the assets of the estate of said decedent; that as such legatee and distributee, there were distributed to the petitioner, on or about April 1, 1946, assets and property of

the decedent and of the decedent's estate of a then fair market value in excess of the amount of the deficiency and/or tax liability involved in this proceeding, together with interest thereon as provided by law.

(j). That by reason of the premises, the petitioner herein became and is now liable as a transferee of the property of the taxpayer, Jennie Wolf, Deceased, and has become and is now answerable to the extent of the amount of said deficiency in income tax, together with interest thereon as provided by law.

Wherefore, it is prayed that petitioner's appeal be denied; that the respondent's determination be approved; and that the petitioner herein be held to be liable at law or in equity as a transferee of the assets of the taxpayer, Jennie Wolf, Deceased.

/s/ CHARLES OLIPHANT, JHP  
Acting Chief Counsel,  
Bureau of Internal  
Revenue.

Of Counsel:

B. H. NEBLETT,  
Division Counsel,

JOHN H. PIGG,

R. G. HARLESS,

Special Attorneys,

Bureau of Internal Revenue.

Received and filed Aug. 7, 1947. T. C. U. S.

[Title of Tax Court and Cause.]

## REPLY

The above-named petitioner, for reply to the allegations affirmatively set out by the respondent in his answer, admits, denies and alleges as follows:

VII(a). Admits the allegations contained in paragraph VII(a) of the answer, except the petitioner denies that the deficiency involved in this proceeding is or was due from Jennie Wolf, Deceased.

(b) and (c). Admits the allegations contained in paragraph VII(b) and VII(c) of the answer.

(d). Denies that the final account mentioned in paragraph VII(d) of the answer was filed on March 29, 1946. Alleges it was filed on February 27, 1946. Admits all the remaining allegations mentioned in said paragraph.

(e). Admits the allegations contained in paragraph VII(e) of the answer.

(f). Admits that the distribution mentioned in paragraph VII(f) of the answer was had in accord with the terms of the will of Jennie Wolf, Deceased, and pursuant to the order referred to in said paragraph, and that said distribution left the Estate of Jennie Wolf, Deceased, without assets. Denies all the remaining allegations contained in said paragraph of the answer.



(g). Admits that the deficiency in income tax involved in this proceeding for the taxable year 1943, in the amount of \$42,273.99, has not been paid. Denies all the remaining allegations contained in paragraph VII(g) of the answer, and particularly denies that the amount of \$42,273.99 or interest thereon, or any other amount or interest thereon is now due and owing to the United States on account of the matters or taxes in controversy in this proceeding.

(h). Admits the allegations contained in paragraph VII(h) of the answer, except petitioner denies that any deficiency or interest thereon in the income tax involved in this proceeding is due or owing to the United States.

(i). Admits that by reason of paragraph eight (8) of the will of the decedent, Jennie Wolf, the petitioner herein was one of the three legatees of said decedent and distributees of the assets of the estate of said decedent; that as such legatee and distributee, there were distributed to the petitioner, on or about April 1, 1946, assets and property of the decedent and of decedent's estate. Denies all of the remaining allegations contained in paragraph VII(i) of the answer, except as in this paragraph next alleged. Alleges that the fair market value as of April 1, 1946, and the appraised value of the said assets and property so distributed to petitioner was in the sum of \$27,466.92 and did not exceed said sum.



(j). Denies the allegations contained in paragraph VII(j) of the answer, and particularly denies that the petitioner is liable as a transferee of the property of the taxpayer, Jennie Wolf, Deceased, and has become or is now answerable to the extent of the amount of the alleged deficiency in income tax, together with interest thereon or in or to any other amount or interest thereon.

VIII. Denies generally and specifically each and every material allegation contained in paragraphs VII(a) to (j), inclusive, of respondent's answer, not hereinbefore especially admitted, qualified or denied.

Wherefore, the petitioner prays that the respondent's determination be disapproved, that the prayer in the answer be denied, and that the prayer in the petition be granted.

/s/ ROBT. T. JACOB,

Counsel for Petitioner.

State of Oregon,

County of Multnomah—ss.

Blossom M. Goldstein, being first duly sworn, says that she is the petitioner above named, that she has read the foregoing reply and is familiar with the statements contained therein, and that the statements contained therein are true, except those

stated to be upon information and belief, and those she believes to be true.

/s/ BLOSSOM M. GOLDSTEIN,

Subscribed and sworn to before me this 10th day of November, 1947.

[Seal] /s/ J. F. JOHNSON,

Notary Public for Oregon.

My Commission expires: 3/28/51.

[Lodged]: Nov. 19, 1947, T.C.U.S.

Filed Nov. 20, 1947.

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[Title of Tax Court and Cause.]

MOTION FOR ORDER GRANTING PERMISSION TO AMEND PETITION

Comes now the petitioner in the above-entitled cause by Robt. T. Jacob, her counsel of record, and moves the Court for an order permitting him to amend her petition by adding to paragraph V of said petition immediately after sub-paragraph (a) of paragraph V a sub-paragraph to be designated (a.1) in form and substance as follows:

(a.1) During the year 1944 said Jennie Wolf instituted proceedings in the Tax Court of the United States against the Commissioner of Internal Revenue by filing in said court a petition, docket number 6263, appealing from a purported deficiency in

income taxes for the calendar year 1941, in which petition said Jennie Wolf, as the petitioner therein, among other things, alleged:

“(a) Petitioner is a member of the partnership of Alaska Junk Company, which said partnership is composed of four individuals, H. J. Wolf, Mrs. J. Wolf, S. Schnitzer and Mrs. R. Schnitzer, each owning a one-fourth interest therein.”

The Commissioner of Internal Revenue filed his answer to said petition in said court and in his answer admitted the above-quoted allegation. Docket numbers 6262, 6264 and 6265 were similar proceedings instituted respectively by Harry J. Wolf, Sam Schnitzer and Rose Schnitzer, and in the petitions in each of these dockets there was an allegation similar to the one above quoted, and in the answer to each said petition the Commissioner admitted said allegation. Thereafter the said proceeding docket number 6263, and the related dockets 6262, 6264 and 6265 were consolidated for trial and tried by the said Tax Court of the United States, and on or about the 23rd day of December, 1946, the said Tax Court of the United States made and entered findings of fact and its opinion, in which findings of fact the said court found:

“The petitioners are husbands and wives and members of a co-partnership, doing business under the firm name and style of Alaska Junk Company at Portland, Oregon. Each Petitioner had a one-fourth interest in the firm. They filed individual in-

come tax returns with the collector of internal revenue for the district of Oregon.

The partnership, Alaska Junk Company, was originally organized by petitioners, H. J. Wolf and S. Schnitzer, in 1911. Its business was the buying and selling of all sorts of salvage metals and materials. The original partnership continued until 1925 or 1926 when the wives of the partners, petitioners Jennie Wolf and Rose Schnitzer, were taken into the firm. That partnership is still in existence except that petitioner Jennie Wolf, the wife of H. J. Wolf, died in April, 1945."

On or about the 24th day of September, 1946, the said Court entered its decisions in each of the said causes and each of the said decisions, less formal parts, date, seal and signature, is as follows:

"Pursuant to the determination of the Court, as set forth in its Memorandum Findings of Fact and Opinion, entered Sept. 23, 1946, it is

Ordered and Decided: That there is no deficiency in income tax for the calendar year 1941."

That the findings and decision in docket 6263 was a final adjudication in favor of said Jennie Wolf and against the Commissioner of Internal Revenue. The interest of Sam Schnitzer, Rose Schnitzer, Harry J. Wolf and Jennie Wolf in said Alaska Junk Company were exactly the same in the calendar years 1942 and 1943 as in the year 1941, and the fact that each of the said persons has said interests in said partnership during said

years has become res judicata and the Respondent ought to be and is estopped to deny the same.

/s/ ROBT. T. JACOB,

Counsel for Petitioner.

Granted June 10, 1948.

/s/ LUTHER A. JOHNSON,

Judge.

Filed June 10, 1948, T.C.U.S.



[Title of Tax Court and Cause.]

ANSWER TO AMENDMENT TO PETITION

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for answer to the amendment to petition filed by the above-named petitioner, admits and denies as follows:

V-(a.1). Admits the allegations contained in subparagraph (a.1) of paragraph V of the petition except those contained in the last two sentences thereof which are denied.

/s/ CHARLES OLIPHANT,  
Chief Counsel, Bureau of  
Internal Revenue.

Of Counsel:

B. H. NEBLETT,  
Division Counsel.

JOHN H. PIGG,  
LEONARD A. MARCUSSEN,  
Special Attorneys,  
Bureau of Internal Revenue.

Received and filed July 28, 1948, T.C.U.S.

Served July 29, 1948.

The Tax Court of the United States  
Washington

Docket No. 14279

BLOSSOM M. GOLDSTEIN,

Petitioner, .

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

### DECISION

Pursuant to Opinion of the Tax Court promulgated July 14, 1949, the respondent filed a computation on October 6, 1949, and the petitioner, on November 7, 1949, filed an acquiescence in the computation as filed by the respondent. Now, therefore, it is

Ordered and Decided: That there is a deficiency in income and victory tax due from this petitioner for the calendar year 1943 in the amount of \$42,273.99.

/s/ LUTHER A. JOHNSON,  
Judge.

Entered Nov. 9, 1949.

Served Nov. 10, 1949.

In the United States Court of Appeals  
for the Ninth Circuit

T. C. Docket No. 14279

BLOSSOM M. GOLDSTEIN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

### PETITION FOR REVIEW

Comes now the petitioner, by his attorneys of record, and respectfully shows this Honorable Court:

#### I.

The petitioner is an individual residing at 3111 S. E. Lambert, Portland, Oregon, and is one of three equal transferees of the residuary estate of Jennie Wolf, deceased. The return for the period here involved was filed by Jennie Wolf with the Collector of Internal Revenue for the District of Oregon.

#### II.

The respondent is the duly appointed, qualified and acting Commissioner of Internal Revenue of the United States and is hereinafter referred to as the "Commissioner."

## III.

The taxes in controversy are income and victory taxes for the calendar year 1943.

## IV.

## Nature of Controversy

For many years prior to and during the taxable year before the court Sam Schnitzer, Harry J. Wolf, Rose Schnitzer and Jennie Wolf were doing business as copartners under the name and style of Alaska Junk Company. During the years 1942 and 1943 Alaska Junk Company was engaged in the business of buying, selling and generally dealing in junk, pipe, tools, machinery, hardware, scrap and other metals, and, as a part of its regular business, made loans and advances to customers and affiliated enterprises, always treating these loans and advances as "accounts receivable" on its books of account.

Morris Schnitzer, a son of Sam Schnitzer, was engaged in a similar business and in 1941 organized the Oregon Electric Steel Rolling Mills (hereinafter referred to as "Oregon Steel") an Oregon corporation, to manufacture steel products. The company's authorized capital was 2,500 shares having a par value of \$100.00 each, a total capital of \$250,000.00. Upon final distribution of this stock the partners of Alaska Junk Company received 1,249 shares and Morris Schnitzer 625 shares.

From October, 1941 to November, 1943 Alaska

Junk Company advanced to Oregon Steel, cash \$327,870.23, paid bills of \$166,340.16 and furnished goods at market prices to the amount of \$347,341.62, making a total of \$841,552.01. All of these items were charged on Alaska Junk Company's books as "accounts receivable" from Oregon Steel. On the books of Oregon Steel these items were entered as "accounts payable." Alaska Junk Company received payments of cash \$114,519.88, received stock of a par value \$124,900.00 and debenture notes of a face value of \$174,000.00 making total receipts of \$413,419.88, which items were credited to said accounts receivable.

Morris Schnitzer and Alaska Junk Company orally agreed that Morris Schnitzer would bear  $\frac{1}{3}$  of the total loss, if any, that might be sustained by Morris Schnitzer and Alaska Junk Company from advances to Oregon Steel over and above the advances credited to stock subscriptions. Alaska Junk Company in turn agreed to bear  $\frac{2}{3}$  of any such loss.

Alaska Junk Company was induced to make the advances, sell goods on credit and pay the bills of Oregon Steel upon a promise of early repayment, based upon engineering estimates of minimum earnings of \$50,000.00 per month and a production schedule to begin early in 1943.

In June, 1943 Morris Schnitzer was inducted into military service and Oregon Steel was unable to obtain competent management. As a result of this and other difficulties the operations were unsue-



cessful, and in November, 1943 ceased. It was then decided by the stockholders to withdraw from the enterprise, and Oregon Steel stock was then sold. Prior to the sale Oregon Steel issued Alaska Junk Company its promissory note for \$427,843.87, the balance of its account receivable, and issued its note of \$26,829.28 to Schnitzer Steel Products Company (Morris Schnitzer). In exchange for these two notes Alaska Junk Company and Morris Schnitzer received a third mortgage note for \$151,000.00. This compromise resulted in a total loss of \$303,625.90 and by reason of the agreement between Morris Schnitzer and Alaska Junk Company, Alaska Junk Company sustained a loss of \$202,350.60, which was charged off as a bad debt.

On the partnerships return for 1943 a deduction of the \$202,350.60 was claimed as a bad debt. It is this amount which the Commissioner has disallowed as a deduction. The Commissioner's contention was upheld by the Tax Court of the United States and petitioner submits that in making its determination the Tax Court was in error.

## V.

The petitioner designates the following points on which he intends to reply on appeal to the United States Court of Appeals for the Ninth Circuit from the decision heretofore entered by the Tax Court of the United States:

1. The tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the

partnership in which petitioner's transferror was a partner was not deductible as a bad debt in computing net income subject to taxation.

2. The Tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the partnership in which petitioner's transferror was a partner was not a bad debt.

3. The Tax Court erred in holding that all of the advances, including said sum of \$202,350.60, of the partnership in which petitioner's transferror was a partner were contributions to capital.

4. The Tax Court erred in not finding and holding that all of said sum of \$202,350.60 was a loan made by the partnership in which petitioner's transferror was a partner.

5. The decision entered by the Tax Court herein is not supported by the evidence, is contrary to the evidence and is in disregard of it.

6. The Tax Court erred in determining that there was a deficiency in income and victory taxes for the calendar year 1943 due from the above named petitioner.

Wherefore, the petitioner petitions that the decision of the Tax Court of the United States be reviewed by the United States Court of Appeals for the Ninth Circuit; that a copy of the record on review be prepared in accordance with law and with the rules of said Court and transmitted to the Clerk of said Court for filing and that appro-

priate action be taken by said Court to review and correct the decision of the Tax Court which petitioner submits is erroneous.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,

Attorneys for Petitioner.

Received and filed Jan. 4, 1950.

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[Title of Court of Appeals and Cause.]

NOTICE OF FILING OF PETITION FOR  
REVIEW

To: Charles Oliphant, Chief Counsel for the Bureau  
of Internal Revenue.

You will please take notice that on the 4th day of January, 1950, the petitioner above named filed with the Clerk of the Tax Court of the United States at Washington, D.C. a Petition for Review by the United States Court of Appeals for the Ninth Circuit of the decision of the Tax Court of the United States heretofore entered in the above entitled proceeding.

A copy of said Petition for Review as filed is attached hereto and served upon you.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES.

Receipt of copy acknowledged Jan. 9, 1950.

Received and filed Jan. 9, 1950.

The Tax Court of the United States  
Washington

[Title of Cause.]

CERTIFICATE

I, Victor S. Mersch, Clerk of The Tax Court of the United States do hereby certify that the foregoing documents, 1 to 13, inclusive, constitute and are all of the original papers and proceedings before The Tax Court of the United States as set forth in the "Designation of Record" except the original exhibits 1-27, incl., 28, 30, 31, 33-36, incl., 65, 66, 72-79, incl.; A-Z, AA-HH, incl., on file in my office as the original record in the proceeding and in which the petitioner in The Tax Court proceeding has initiated an appeal as above numbered and entitled, together with a true copy of the docket entries in said Tax Court proceeding, as the same appear in the official docket book in my office.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia, this 23rd day of January, 1950.

[Seal]      /s/ VICTOR S. MERSCH,  
Clerk.

[Endorsed]: No. 12474. United States Court of Appeals for the Ninth Circuit. Blossom M. Goldstein, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Petition to Review a Decision of The Tax Court of the United States.

Filed February 7, 1950.

/s/ PAUL P. O'BRIEN,  
Clerk of the United States Court of Appeals for  
the Ninth Circuit.



In the United States Court of Appeals  
for the Ninth Circuit

T. C. Docket No. 14208

SAM SCHNITZER,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

T. C. Docket No. 14209

ESTATE OF HARRY J. WOLF, Deceased, by  
MONTE L. WOLF, Administrator de bonis  
non with the will annexed of said Estate,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

T. C. Docket No. 14278

MONTE L. WOLF,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

T. C. Docket No. 14279

BLOSSOM M. GOLDSTEIN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14280

CHARLOTTE C. COHON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14372

ESTATE OF JENNIE WOLF, Deceased, by  
MONTE L. WOLF, Administrator de bonis  
non with the will annexed of said Estate,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

## MOTION TO CONSOLIDATE APPEALS

The above named petitioners on review and each of them, acting by and through their attorneys of record, hereby move this court to consolidate the above entitled proceedings for purposes of the printed record on appeal, the briefing, the hearing,

the argument, the decision and for all other purposes connected with the final disposition of said proceedings on review.

This motion is based on the grounds that all of the above entitled proceedings were consolidated for trial below in the Tax Court, that the Tax Court made but one set of findings of fact and rendered but one opinion in connection with all of these cases, that each of these cases involves the same facts, that each of the petitioners on review was either a partner or is now the transferee of a decedent who was a partner in a partnership known as the Alaska Junk Company, that the sole question for decision concerns the deductibility of a bad debt by said Alaska Junk Company, and that the decision on this single point is determinative of the income tax liability of each of said partners or said transferees of partners who are the petitioners herein.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,

917 Public Service Building,  
Portland 4, Oregon.

I, Randall S. Jones, being on oath first duly sworn, depose and say:

That on the 13th day of February, 1950, I served the foregoing Motion to Consolidate Appeals upon Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, by on said day depositing a duly certified copy thereof in the United

States mails with full postage and registration charges prepaid, addressed to Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, Internal Revenue Building, Washington, D. C. Said papers were deposited in the United States mails at the Federal Post Office, S. W. Sixth and Main Streets, Portland 4, Oregon.

/s/ RANDALL S. JONES.

Subscribed and sworn to before me this 13th day of February, 1950.

[Seal] /s/ JACQUELINE MOHLAND,  
Notary Public for Oregon.

My commission expires: 9-22-52.

So Ordered:

/s/ WILLIAM DENMAN,  
Chief Judge.

/s/ HOMER BONE,

/s/ WM. E. ORR,

U. S. Circuit Judge.

[Endorsed]: Filed Feb. 15, 1950.

[Title of Court of Appeals and Causes.]

STATEMENT OF POINTS ON WHICH  
PETITIONERS INTEND TO RELY

The petitioners on review hereby enumerate the points on which they intend to rely on appeal and which are as follows:

1. The Tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the partnership in which petitioners were partners was not a bad debt and not deductible in computing the net income of said partnership and petitioners' net income subject to taxation for the taxable year 1943.

2. The Tax Court erred in holding that the total, or any amount in excess of \$125,000.00, representing bills paid for, cash advanced to, and goods sold to Oregon Electric Steel Rolling Mills by the partnership in which petitioners or their transferrors were partners, constituted a contribution to the capital of said Oregon Electric Steel Rolling Mills.

3. The Tax Court erred in not finding and holding that all and every part of said sum of \$202,350.60 was a debt owed to the partnership in which petitioners were partners.

4. The decision entered by the Tax Court herein is contrary to the law, the Tax Court's findings of fact, and the evidence; and is not supported by said findings of fact or the evidence and is in disregard of both said findings of fact and the evidence.



5. The Tax Court erred in failing to include in its findings material facts clearly established by the evidence which further show that the bills paid, cash advanced and goods sold to Oregon Electric Steel Rolling Mills constituted an indebtedness owed to the partnership.

6. The Tax Court erred in admitting respondent's exhibits O, P, Q, U, V, AA, FF, GG and HH over objections of petitioner for the reasons set forth respectively on pages 120, 121, 122, 129, 134, 137, 495, 589-591, 621 and 636, 639 and 640 of the *Report's* Transcript of the Proceedings before said court.

7. The Tax Court erred in receiving oral testimony adduced by respondent over objections of the petitioners as set forth in those portions from the Reporter's Transcript of the Proceedings before said court which the petitioners have designated for inclusion in the Printed Record.

8. The Tax Court erred in sustaining objections of the respondent to questions asked by petitioners and to oral testimony offered by petitioners, which questions, objections and rulings thereon are set forth in those portions from the Reporter's Transcript of the Proceedings before said court which

the petitioners have designated for inclusion in the Printed Record.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,

917 Public Service Bldg.,  
Portland 4, Oregon.

I, Randall S. Jones, being on oath first duly sworn, depose and say:

That on the 13th day of February, 1950, I served the Statement of Points on which Petitioners Intend to Rely upon Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, by on said day depositing a duly certified copy thereof in the United States mails with full postage and registration charges prepaid, addressed to Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, Internal Revenue Building, Washington, D. C. Said papers were deposited in the United States mails at the Federal Post Office, S. W. Sixth and Main Streets, Portland 4, Oregon.

/s/ RANDALL S. JONES.

Subscribed and sworn to before me this 13th day of February, 1950.

[Seal] /s/ JACQUELINE MOHLAND,  
Notary Public for Oregon.

My commission expires: 9-22-52.

[Endorsed]: Filed Feb. 15, 1950.



No. 12475

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United States  
Court of Appeals  
For the Ninth Circuit.

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CHARLOTTE C. COHON,

Petitioner,

*vs.*

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

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Transcript of Record

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Petition to Review a Decision of the Tax Court  
of the United States

FILED

APR 6 1950

PAUL P. O'BRIEN,  
CLERK





No. 12475

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United States  
Court of Appeals  
For the Ninth Circuit.

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CHARLOTTE C. COHON,

Petitioner,

*vs.*

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

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Transcript of Record

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Petition to Review a Decision of the Tax Court  
of the United States



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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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## NAMES AND ADDRESSES OF ATTORNEYS

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Portland 4, Oregon,

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CHARLES OLIPHANT,

Acting Chief Counsel,

Bureau of Internal Revenue,

B. H. NEBLETT,

Division Counsel,

JOHN H. PIGG,

R. G. HARLESS,

Special Attorneys,

Bureau of Internal Revenue.



The Tax Court of the United States

T. C. Docket No. 14280

CHARLOTTE C. COHON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

### PETITION

The above-named petitioner hereby petitions the above-entitled court for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his Notice of Deficiency (Bureau Symbols IT:90D:DLA), dated March 4, 1947, and as a basis of her proceeding alleges as follows:

#### I.

The petitioner, an individual, residing at 7825 S. W. Reed College Place, Portland, Oregon, is one of three equal transferees of the residuary estate of Jennie Wolf, Deceased. The returns for the periods here involved were filed by Jennie Wolf with the Collector for District of Oregon.

#### II.

The Notice of Deficiency (a copy of which is attached and marked Exhibit A) was mailed to the

petitioner from Seattle, Washington, under date of March 4, 1947.

### III.

The taxes in controversy are income taxes for the calendar years 1942 and 1943, and the amount in controversy does not exceed \$42,273.99, which sum is equal to the amount of deficiency asserted. The petitioner contends that at all times during the calendar years 1942 and 1943, Jennie Wolf was a partner in The Alaska Junk Company with an interest therein equal to that of her husband, Harry J. Wolf. Said partnership interest of Jennie Wolf is in issue before this Court in the appeal hereinafter mentioned, and in the event this Court in said appeal should determine that Jennie Wolf was not such partner during said calendar years, the petitioner claims that she is entitled to a refund of \$12,316.99 which is one-third of the amount of \$36,950.97 paid by said Jennie Wolf within three years of the mailing of said Notice of Deficiency as income and victory taxes on account of her distributive share of the net income of said partnership for the calendar years of 1942 and 1943.

### IV.

The determination of the tax set forth in said Notice of Deficiency is based upon the following errors:

(a) The Commissioner erred in disallowing as a deduction of The Alaska Junk Company in the calendar year 1943 the sum of \$202,350.60 as (1) a

bad debt owed to The Alaska Junk Company by the Oregon Electric Steel Rolling Mills which became worthless in said calendar year, or (2) as a loss deductible under the provisions of Sec. 23 (e), IRC.

(b) The Commissioner erred in including an additional \$50,587.65 in the Income Tax Net Income and Victory Tax Net Income of said Jennie Wolf for the calendar year 1943 as a result of his said disallowance of the said sum of \$202,350.60 as a deduction of The Alaska Junk Company for said calendar year.

#### V.

The facts upon which the petitioner relies as the basis of this proceeding are as follows:

#### Re Bad Debt Loss

(a) At and during the calendar years 1942 and 1943, and for a great many years prior thereto, Sam Schnitzer, Rose Schnitzer, Harry J. Wolf and Jennie Wolf were co-partners under the names and styles of The Alaska Junk Company and Schnitzer-Wolf Machinery Company, and as such co-partners were engaged in the business of buying, selling and generally dealing in junk, new and second hand pipe, tools, machinery, hardware, metal and metal products of every character, and in promoting and financing business enterprises of a nature related to the other said activities of said partnership, and the principal place of business of said partners was in Portland, Oregon. During all said times each

of the said persons owned a one-quarter interest in the business and property of said partnership, which said partnership is hereinafter referred to as The Alaska Junk Company.

(b) At and during all the times hereinafter mentioned the Oregon Electric Steel Rolling Mills, hereinafter called the corporation, was a corporation having an authorized capital stock of 2500 shares consisting of common stock of a par value of \$100.00 each. Sam Schnitzer and Harry J. Wolf each subscribed to a portion of the capital stock, which portion was subsequently issued and thereupon immediately reissued so as to divide it equally among said four partners. Thereafter additional stock was issued in substantially equal amounts to each of the four partners. Said corporation was fully paid for all said stock. The balance of the issued stock of said corporation was owned by other persons, Morris Schnitzer, son of Sam Schnitzer and Rose Schnitzer, owned all of the said balance except three shares.

(c) Said Morris Schnitzer at and during all times hereinafter mentioned was engaged in Portland, Oregon in the business of buying and selling new and used iron, steel, tools and machinery and conducted such business under the name and style of the Schnitzer Steel Products Co.

(d) In the course of its business The Alaska Junk Company between October 22, 1941 and November 22, 1943, on an open account, at the instance



and request of said corporation, advanced money to said corporation, either directly or by making payments on its account to its creditors, purchased and furnished it with merchandise charging the cost thereof to it, and sold goods, wares and merchandise to it at the regular prices charged by The Alaska Junk Company to the trade in general. On November 26, 1943 the balance due and owing to The Alaska Junk Company from said corporation on said open account was \$428,132.13.

(e) In consideration of said open account being credited with the sum of \$174,000.00 the said corporation made, executed and delivered to The Alaska Junk Company one hundred seventy-four (174) First Debentures (unsecured) in the total amount of \$174,000.00, bearing interest at 8% per annum, and on July 14, 1943 said Alaska Junk Company credited said open account with said amount of \$174,000.00, and charged its "Stocks and Bonds" account with a like sum. For a valuable consideration seventy-five (75) such debentures in the sum of \$75,000.00 were also executed and delivered by said corporation to Morris Schnitzer. No payments of either principal or interest were ever made on any of said debentures.

(f) Soon after the organization of said corporation, The Alaska Junk Company and Morris Schnitzer entered into a contract of guaranty whereby it was agreed that in the event a loss should be sustained by The Alaska Junk Company as a result of its extending credit to said corpora-



tion, Morris Schnitzer would pay to The Alaska Junk Company so much of any such loss as should exceed two-thirds of the total combined losses of himself and The Alaska Junk Company sustained on account of the extension of credit to said corporation by himself and The Alaska Junk Company, and a corresponding guaranty was made by The Alaska Junk Company to Morris Schnitzer to the extent of one-third of the total combined losses of said parties sustained through the extension of credit to said corporation.

(g) The idea for the establishment of said corporation was conceived by Morris Schnitzer and from its inception to July 17, 1943 he acted as its president and manager. On said date he was inducted into the armed service of the United States and this left the corporation without a directing head sufficiently informed and capable of carrying out the purposes of the corporation. Extended and repeated efforts were made to secure a suitable manager to take his place. None could be found. None of the remaining stockholders of said corporation or partners of The Alaska Junk Company were able to properly manage the plant. Its operation bogged down. There was a \$678,843.70 mortgage against its real estate. It owed \$149,650.00 for which its inventories were security, and in addition to the sums it owed The Alaska Junk Company and Morris Schnitzer, it owed \$190,684.06 on open accounts. It lost money, became unable to pay its debts, and it became apparent that it would be

impossible for it to carry on and operate profitably. Thereupon many industrialists of large financial ability were solicited in repeated efforts to find some person or organization that would take over the interests of The Alaska Junk Company and Morris Schnitzer in said corporation under such terms as would save them from loss, or at least, under terms that would result in as little loss to them as possible. Including those solicited were Kenneth E. Hall and A. M. Mears, then of the Hesse-Ersted Iron Works. After extended negotiations an agreement was made by and between said Hall, Mears, The Alaska Junk Company, and Morris Schnitzer, by his attorney-in-fact, Sam Schnitzer, whereby said Hall and Mears agreed to purchase the outstanding stock of said corporation at a nominal sum and thereafter to cause said corporation to execute and deliver a promissory note to The Alaska Junk Company and Morris Schnitzer in the sum of \$249,000.00 to be secured by a second mortgage upon its properties in payment of all said debentures, and to execute and deliver a promissory note to said persons in the sum of \$151,000.00 secured by a third mortgage upon said properties in compromise and full payment of the balance due on said open account and in complete satisfaction of a debt of \$26,493.77 then due and owing from said corporation to Morris Schnitzer. The Alaska Junk Company entered into said agreement for the reason that it gave The Alaska Junk Company the best opportunity it could find to realize the greatest possible amount on the obligations owed to it by said corporation.

(h) As evidence of the correct balance due The Alaska Junk Company on its said open account a demand promissory note in the amount of said balance was executed and delivered by said corporation to The Alaska Junk Company, and as evidence of the correct amount of said debt owed by said corporation to Morris Schnitzer a demand promissory note in the amount of said debt was executed and delivered by said corporation to Sam Schnitzer, the attorney-in-fact for Morris Schnitzer.

(i) On November 26, 1943, subsequent to the execution and delivery of the demand notes mentioned in paragraph V (h), all of the issued stock of said corporation was sold to said Hall and Mears and transferred to them or their order pursuant to the agreement mentioned in paragraph V (g); and thereafter said corporation executed and delivered promissory notes and a second and a third mortgage, and the same were accepted by The Alaska Junk Company and Morris Schnitzer, by his said attorney-in-fact, all in accordance with said agreement.

(j) Up the receipt of said promissory note and second mortgage for the amount of \$249,000.00 all of the said debentures were returned to said corporation as fully paid and satisfied, and The Alaska Junk Company credited its said open account with \$142,200.33, which was its pro-rata share of the said promissory note and third mortgage for \$151,000.00, and pursuant to said guaranty agreement

charged Morris Schnitzer with \$83,581.20 and credited said open account with an equal amount, thereby reducing the balance of said open account to \$202,350.60, which balance became worthless within the calendar year 1943, because under the terms of the settlement with said corporation embodied in the agreement mentioned in paragraph V (g) no further amount could be realized on said unpaid balance from the corporation, and the said sum of \$83,581.20 was the entire amount for which Morris Schnitzer was liable under the said guaranty. On December 31, 1943, The Alaska Junk Company charged off the said balance as a bad debt, and nothing has since been received thereon.

(k) On account of the matters and things hereinabove stated The Alaska Junk Company sustained a bad debt or business loss in the calendar year 1943 in the sum of \$202,350.60.

(l) The Commissioner arbitrarily considered that the said unpaid and worthless balance of \$202,350.60 represented a contribution by The Alaska Junk Company to the capital of said corporation. Petitioner is informed, believes and therefore alleges that there was no intention at any time by any of the said partners, that the said amount, or any portion thereof, should be a capital contribution to said corporation, but on the contrary it was the intention of The Alaska Junk Company that it was extending credit and that the full balance shown by its said open account would be repaid to it by said corporation.



## Re Refund

(m) Said Jennie Wolf was the wife of said Harry J. Wolf and the mother of the petitioner, Blossom M. Goldstein and Monte L. Wolf. Jennie Wolf died on April 8, 1945, and left a will which was duly admitted to probate by an order of the Circuit Court of the State of Oregon for the County of Multnomah, Probate Department, made and entered on April 18, 1945, in the Matter of Estate of Jennie Wolf, Deceased, Probate No. 53880. By the terms of said will said Jennie Wolf directed that her funeral expenses, just debts, estate and inheritance taxes be paid, bequeathed specific articles of jewelry, household furniture, fixtures, linens, silverware, and certain specified sums of money, and then disposed of all the rest, residue and remainder of her property and estate pursuant to the eighth paragraph of said will. The second and eighth paragraphs of said will read as follows:

“Second: I have a husband named Harry J. Wolf. I have three living children, whose names and the date of their births are as follows, to-wit: (1) Monte L. Wolf, who was born on April 5, 1909; and (2) Charlotte C. Cohon—nee Wolf, who was born on September 8, 1911; and (3) Blossom M. Goldstein—nee Wolf, who was born on July 8, 1919.

“Eighth: I give and bequeath and devise all of the rest, residue and remainder of my property and estate—real and personal and mixed, and wheresoever situated and whether acquired before or after



making this will—in equal shares to my above named three children.”

There was no person named in said will as a child of Jennie Wolf other than those named in said second paragraph, and she had no other children.

(n) Said Harry J. Wolf, was duly appointed the executor of said will and estate, qualified as such, and administered the estate. He filed his final account, which was duly approved and distribution was ordered by said Court on March 29, 1946. Distribution was thereupon made of all the property and estate of said Jennie Wolf, Deceased, that remained in the hands of said executor, and by order of said Court duly made, entered and effective on April 1, 1946, the administration of said estate was fully and completely closed and Harry J. Wolf was discharged and released as executor of said estate. There has been no executor of said will or estate or personal representative of said Jennie Wolf, Deceased, since the date last mentioned; and petitioner is informed, believes and therefore alleges that under the law and practice of the State of Oregon said Harry J. Wolf, by virtue of the order last mentioned, was on said date completely and forever divested of any and all right, power or authority to in any way further act for or on behalf of the said estate which was at the same time fully and completely closed as aforesaid.

(o) The petitioner is informed, believes and therefore alleges that in determining the taxable in-

come of said Harry J. Wolf for the calendar years 1942 and 1943 the Commissioner refused to recognize that Jennie Wolf was a partner during said calendar years in the said business carried on under the name of The Alaska Junk Company with an interest therein equal to that of Harry J. Wolf, although the Commissioner had recognized her as such partner for many years prior thereto, and that based on his said refusal to recognize her as such partner during said years he treated her distributive share of the net profits of said partnership for said years as income of Harry J. Wolf and determined a deficiency in the income tax liability of said Harry J. Wolf for said calendar years in the sum of \$151,049.05, and that said Harry J. Wolf has filed with the Clerk of this Court, or at least, has mailed to him for filing, an appeal to this Court wherein said Harry J. Wolf alleged that Jennie Wolf was a partner, with such interest, during said calendar years and that the Commissioner erred in refusing to recognize her as such.

(p) In the event the issue referred to in paragraph V (o) should be determined by this Court adversely to said contentions of said Harry J. Wolf, the said Jennie Wolf will have over-paid her income and victory taxes for said calendar years by the sum of \$36,950.97.

(q) All of the specific and pecuniary bequests made by said Jennie Wolf in her said will were paid in full, and the entire amount of said sum of \$36,950.97 was paid on said income and victory

taxes in diminution of the interests of petitioner, Blossom M. Goldstein, and Monte L. Wolf as the residuary legatees under said will of said Jennie Wolf, Deceased; and in the event of such an adverse determination on said partnership issue, petitioner as a transferee of said Jennie Wolf would be entitled to a refund of one-third of the resultant overpayment as her portion thereof, to-wit: she would be entitled to a refund of \$12,316.99.

(r) None of the foregoing allegations are in any way intended as an admission that the Commissioner was correct in his refusal to recognize said partnership interest of Jennie Wolf, and paragraphs (m) through (q) are included herein only to protect the petitioner's interests as a claimant in the event this Court should determine said partnership issue in said appeal adversely to the interests of Harry J. Wolf.

Wherefore, petitioner prays that this Court may hear this proceeding and determine that Jennie Wolf paid her taxes in full for all years in question and that there is no deficiency in her income and/or victory taxes due from petitioner for said years, and petitioner further prays that this cause not be determined by this Court prior to its determination of said partnership issue in said appeal of Harry J. Wolf, and if said issue is determined adversely to the interests of said Harry J. Wolf, then and in such event, that this Court determine that Jennie Wolf made an overpayment of her income and victory taxes for the calendar years in question in the

sum of \$36,950.97, and that she paid the same within three years prior to the mailing of said Notice of Deficiency, and that the petitioner's share in such overpayment, if an overpayment is determined, is \$12,316.99, together with interest thereon as provided by law, and petitioner also prays for such further relief as may be just and proper in the premises.

/s/ ROBERT T. JACOB,  
Counsel for Petitioner.

State of Oregon,  
County of Multnomah—ss.

Charlotte C. Cohon, being first duly sworn, says that she is the petitioner above named; that she has read the foregoing petition and is familiar with the statements contained therein, and that the statements contained therein are true, except those stated to be upon information and belief, and those she believes to be true.

/s/ CHARLOTTE C. COHON,

Subscribed and sworn to before me this 26th day of May, 1947.

[Seal] /s/ J. F. JOHNSON,  
Notary Public for Oregon.

My Commission expires March 28, 1951.



## Exhibit A

Treasury Department  
Internal Revenue Service  
Seattle 1, Washington

March 4, 1947.

Office of Internal Revenue Agent in Charge, Seattle  
Division, 305A 1331 Third Avenue Building.

IT:90D:DLA

Mrs. Charlotte C. Cohon  
7825 S. W. Reed College Place  
Portland, Oregon

Dear Mrs. Cohon:

You are advised that the determination of the income tax liability of the Estate of Jennie Wolf, deceased, 900 S. W. First Avenue, Portland, Oregon, for the taxable year ended December 31, 1943, discloses a deficiency of \$42,273.99, as shown in the statement attached. The amount of the deficiency stated, plus interest as provided by law, constituting your liability as transferee of assets of said Estate of Jennie Wolf, deceased, will be assessed against you.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days (not counting Saturday, Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter,



you may file a petition with the Tax Court of the United States, at its principal address, Washington 25, D. C., for a redetermination of the deficiency or deficiencies.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, Seattle 1, Washington for the attention of IT:90D:DLA. The signing and filing of this form will expedite the closing of the return(s) by permitting an early assessment of the deficiency or deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

JOSEPH D. NUNAN, JR.

Commissioner.

By /s/ S. R. STOCKTON,

Internal Revenue Agent in  
Charge.

DLA:mts

Enclosures:

Statement

Form of waiver.

IT :90D:DLA

Charlotte C. Cohon, Transferee

Statement

Estate of Jennie Wolf, Deceased, Transferor  
900 S. W. First Avenue  
Portland, Oregon

Tax liability for the taxable year ended December 31, 1943.

Mrs. Charlotte C. Cohon, Transferee  
7825 S. E. Reed College Place  
Portland, Oregon

	Deficiency
Income tax .....	\$ 42,273.99

The records of this office indicate that assets of the above-named decedent's estate were transferred to you on or about April 1, 1946.

The above-stated amount represents your liability as a transferee of assets of the Estate of Jennie Wolf, deceased, 900 S. W. First Avenue, Portland, Oregon, for a deficiency in income tax due from the Estate of Jennie Wolf, deceased, for the taxable year ended Decembr 31, 1943.

Adjustments to Net Income

	Income Tax Net Income	Victory Tax Net Income
Net income as disclosed by return .....	\$ 52,654.75	\$ 56,514.91
Unallowable deductions and additional income:		
(a) Income from partnership .....	50,587.65	50,587.65
Net income adjusted .....	\$103,242.40	\$107,102.56

Explanation of Adjustments

(a) It is held after examination of the 1943 return filed by the partnership, Alaska Junk Co., that the distributive share of Jennie Wolf, deceased, of the income from that partnership was \$107,101.58. Reported on the return, \$56,513.93. Additional income from partnership, \$50,587.65.

## Computation of Income and Victory Tax

Income tax net income, adjusted .....	\$103,242.40
Less: Personal exemption .....	None
Surtax net income .....	\$103,242.40
Less: Earned income credit .....	300.00
Balance subject to normal tax .....	\$102,942.40
Normal tax at 6% on \$102,942.40.....	\$ 6,176.54
Surtax on \$103,242.40 .....	61,701.50
Total income tax .....	\$ 67,878.04
Victory tax net income adjusted .....	\$107,102.56
Less: Specific exemption .....	624.00
Income subject to victory tax .....	\$106,478.56
Victory tax before credit, 5% of \$106,478.56 .....	\$ 5,323.93
Less: Victory tax credit .....	500.00
Net victory tax .....	4,823.93
Net income tax and victory tax .....	\$ 72,701.97
Income tax for 1942 .....	\$ 26,091.94
Amount of net income tax and victory tax .....	\$ 72,701.97
Forgiveness feature:	
(a) Amount of income tax for 1942.....	\$ 26,091.94
(b) Amount forgiven ( $\frac{3}{4}$ of (a) ).....	19,568.95
(c) Amount unforgiven .....	6,522.99
Total income and victory tax liability .....	\$ 79,224.96
Income and victory tax liability disclosed by return, Account No. 353534 .....	36,950.97
Deficiency of income tax .....	\$ 42,273.99

Received and Filed May 29, 1947.

[Title of Tax Court and Cause.]

## ANSWER

Comes Now the Commissioner of Internal Revenue, by his attorney, Charles Oliphant, Acting Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed herein, admits, denies and alleges as follows:

### I.

Admits the allegations contained in paragraph I of the petition.

### II.

Admits the allegations contained in paragraph II of the petition.

### III.

Admits that the taxes in controversy are, in part, income taxes for the calendar years 1942 and 1943; that the amount of the taxes so in controversy, exclusive of interest as provided by law, is, to wit: \$42,273.99, and that the alleged partnership interest of the decedent, Jennie Wolf, in the business known and carried on under the name of Alaska Junk Company during the years 1942 and 1943 is in controversy before this Court. Denies the remaining allegations contained in paragraph III of the petition, but admits that petitioner makes the contentions as set forth in said paragraph. Alleges that said amount of, to wit: \$42,273.99, consists, in part, of victory tax for the year 1943; that the income

tax liability of the decedent, Jennie Wolf, for the year 1942, is involved in this proceeding only by reason of the forgiveness feature of section 6 of the Current Tax Payment Act of 1943; that no part of the deficiency in income and victory tax as determined by respondent to be due from petitioner's transferror, the Estate of Jennie Wolf, Deceased, for the taxable year 1943, in the amount of, to wit: \$42,273.99, arises out of or is attributable to any adjustment made by respondent to or in respect of the net income as reported by petitioner's said transferror and/or said transferror's decedent, Jennie Wolf, for the taxable year 1942, and that the alleged partnership interest of the decedent, Jennie Wolf, in the business known and carried on under the name of Alaska Junk Company during the years 1942 and 1943 is in issue before this Court in the related proceedings entitled Harry J. Wolf, Docket No. 14209, and Sam Schnitzer, Docket No. 14278; also, in the related transferree proceedings entitled Blossom M. Goldstein, Docket No. 14279, and Monte L. Wolf, Docket No. 14278.

#### IV.

(a) and (b). Denies that he erred in his determination of the deficiency shown by the notice of deficiency from which petitioner's appeal is taken. Specifically denies that he erred in the manner and form as alleged in paragraph IV(a) and (b) of the petition.



## V.

(a). Denies the allegations contained in paragraph V(a) of the petition, except to the extent that in the event the decisions of this Court in the pending related cases of Harry J. Wolf, Docket No. 14209, and Sam Schnitzer, Docket No. 14208, should be adverse to respondent, i.e., the Court's decisions in those cases should be predicated upon his finding and holding by said Court that the decedent, Jennie Wolf, was, during the taxable years 1942 and 1943, a valid and bona fide partner in the business known and carried on under the name of Alaska Junk Company, and said decisions shall have become final, then and in that event, and upon that condition only, the respondent admits the allegations contained in said paragraph V(a) of the petition.

(b) to (j), inclusive. For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth or falsity thereof, denies the allegations contained in paragraph V(b) to (j), inclusive, of the petition.

(k). Denies the allegations contained in paragraph V(k) of the petition.

(l). Admits that he, the Commissioner, considered the balance of \$202,350.60 as a capital investment. Denies the remaining allegations contained in paragraph V(l) of the petition.

(m). Admits the allegations contained in paragraph V(m) of the petition.

(n). Admits the allegations contained in paragraph V(n) of the petition, except that it is denied that said Harry J. Wolf is now divested of any right, power or authority to act for and on behalf of said estate.

(o). Admits that he, the Commissioner, in determining the taxable income of said Harry J. Wolf, for the calendar years 1942 and 1943, refused to recognize that Jennie Wolf was a partner during said calendar years in the business carried on under the name of Alaska Junk Company with an interest therein equal to that of Harry J. Wolf; that based on his said refusal to recognize the decedent, Jennie Wolf, as such partner during said years, he treated her alleged distributive share of net profits of said business for said years as income of Harry J. Wolf and determined a deficiency in the income and victory tax liability of said Harry J. Wolf for the year 1943 in the amount of, to wit: \$151,049.05; and that said Harry J. Wolf has filed with this Court his petition, at Docket No. 14209, as aforesaid, wherein he alleged that the decedent, Jennie Wolf, was a partner, with such interest, during said years, and that the Commissioner erred in refusing to recognize her as such. Denies the remaining allegations contained in paragraph V(o) of the petition.

(p). Admits that in the event the issue referred to in paragraph V(o) of the petition, which said issue is presented in the pending proceeding en-

titled Harry J. Wolf, Docket No. 14209, as aforesaid, should be determined by this Court adversely to the contentions of said Harry J. Wolf, the decedent, the said Jennie Wolf, will have overpaid her income and victory tax for the year 1943. For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth or falsity thereof, denies the remaining allegations contained in paragraph V(p) of the petition.

(q). Admits that all of the specific and pecuniary bequests made by said Jennie Wolf in her said will were paid in full. Denies the remaining allegations contained in paragraph V(q) of the petition.

(r). Because of the absence of any allegation of fact therein, respondent neither admits nor denies the statements set forth in paragraph V(r) of the petition.

## VI.

Denies generally and specifically each and every material allegation contained in the petition, not hereinbefore specifically admitted, qualified, or denied.

## VII.

For further answer to the petition herein, respondent alleges as follows:

(a). That the taxpayer, namely: Jennie Wolf,

now deceased, and formerly of Portland, Oregon, from whom respondent determined the deficiency involved in this proceeding to be due, died on, to wit: April 8, 1945, a resident of the State of Oregon; that said decedent died testate; that said decedent's will was duly admitted to probate by order of the Circuit Court of the State of Oregon for the County of Multnomah, Probate Department, made and entered April 18, 1945.

(b). That by the terms of said will, said decedent directed payment of all expenses and debts, made specific bequests and then disposed of all the rest, residue and remainder of her property and estate, pursuant to paragraph eight (8) of said will. The second and eighth paragraphs of said will read as follows:

“Second: I have a husband named Harry J. Wolf; I have three living children, whose names and the date of their births are as follows, to-wit. (1) Monte L. Wolf, who was born on April 5, 1909; and (2) Charlotte C. Cohon—nee Wolf, who was born on September 8, 1911; and (3) Blossom M. Goldstein—nee Wolf, who was born on July 8, 1919.

\* \* \*

“Eighth: I give and bequeath and devise all of the rest, residue and remainder of my property and estate—real and personal and mixed, and wheresoever situated and whether acquired before or after



making this Will—in equal shares to my above named three children.”

(c). That the petitioner herein is one of the three children mentioned in paragraph eight (8) of said will as a residuary legatee.

(d). That a final account by the duly appointed and authorized executor of the Estate of Jennie Wolf, Deceased, was filed with the said court on March 29, 1946, and was duly approved, and distribution was ordered by said court on March 29, 1946.

(e). That pursuant to the order of said court above referred to, distribution was thereupon made of all the property and estate of said Jennie Wolf, Deceased, that remained in the hands of said executor and by order of said court duly made, entered and effective on April 1, 1946, the administration of said estate was fully and completely closed and said executor was discharged and released as executor of said estate.

(f). That the distribution in accord with the terms of the will of said decedent, and pursuant to said order of said court, had the effect of rendering the Estate of Jennie Wolf, Deceased, insolvent.

(g). That the deficiency in income tax involved in this proceeding for the taxable year 1943, in the amount of \$42,273.99, has not been paid, and that the same is now due and owing to the United



States, together with interest thereon, as provided by law.

(h). That at the time of her death, testate, on, to wit: April 8, 1945, as aforesaid, the decedent, Jennie Wolf, was the owner of property and assets of the then fair market value in excess of the deficiency in income tax involved in this proceeding, together with interest thereon as provided by law.

(i). That by reason of paragraph eight (8) of the said will of decedent, as aforesaid, the petitioner herein was one of the three legatees of the decedent and distributees of the assets of the estate of said decedent; that as such legatee and distributee, there were distributed to the petitioner, on or about April 1, 1946, assets and property of the decedent and of the decedent's estate of a then fair market value in excess of the amount of the deficiency and/or tax liability involved in this proceeding, together with interest thereon as provided by law.

(j). That by reason of the premises, the petitioner herein became and is now liable as a transferee of the property of the taxpayer, Jennie Wolf, Deceased, and has become and is now answerable to the extent of the amount of said deficiency in income tax, together with interest thereon as provided by law.

Wherefore, it is prayed that petitioner's appeal be denied; that the respondent's determination be approved; and that the petitioner herein be held

to be liable at law or in equity as a transferee of the assets of the taxpayer, Jennie Wolf, Deceased.

/s/ CHARLES OLIPHANT, JHP,  
Acting Chief Counsel, Bureau  
of Internal Revenue.

Of Counsel:

B. H. NEBLETT,  
Division Counsel,

JOHN H. PIGG,  
R. G. HARLESS,  
Special Attorneys,  
Bureau of Internal Revenue.

Received and filed Aug. 7, 1947, T.C.U.S.

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[Title of Tax Court and Cause.]

## REPLY

The above named petitioner, for reply to the allegations affirmatively set out by the respondent in his answer, admits, denies and alleges as follows:

### VII.

(a). Admits the allegations contained in paragraph VII(a) of the answer, except the petitioner denies that the deficiency involved in this proceeding is or was due from Jennie Wolf, Deceased.

(b) and (c). Admits the allegations contained in paragraph VII (b) and VII(c) of the answer.

(d). Denies that the final account mentioned in paragraph VII(d) of the answer was filed on March 29, 1946. Alleges it was filed on February 27, 1946. Admits all the remaining allegations mentioned in said paragraph.

(e). Admits the allegations contained in paragraph VII(e) of the answer.

(f). Admits that the distribution mentioned in paragraph VII(f) of the answer was had in accord with the terms of the will of Jennie Wolf, Deceased, and pursuant to the order referred to in said paragraph, and that said distribution left the Estate of Jennie Wolf, Deceased, without assets. Denies all the remaining allegations contained in said paragraph of the answer.

(g). Admits that the deficiency in income tax involved in this proceeding for the taxable year 1943, in the amount of \$42,273.99, has not been paid. Denies all the remaining allegations contained in paragraph VII(g) of the answer, and particularly denies that the amount of \$42,273.99 or interest thereon, or any other amount or interest thereon is now due and owing to the United States on account of the matters or taxes in controversy in this proceeding.

(h). Admits the allegations contained in paragraph VII(h) of the answer, except petitioner de-

nies that any deficiency or interest thereon in the income tax involved in this proceeding is due or owing to the United States.

(i). Admits that by reason of paragraph eight (8) of the will of the decedent, Jennie Wolf, the petitioner herein was one of the three legatees of said decedent and distributees of the assets of the estate of said decedent; that as such legatee and distributee, there were distributed to the petitioner, on or about April 1, 1946, assets and property of the decedent and of decedent's estate. Denies all the remaining allegations contained in paragraph VII(i) of the answer, except as in this paragraph next alleged. Alleges that the fair market value as of April 1, 1946, and the appraised value of the said assets and property so distributed to petitioner was in the sum of \$27,723.42 and did not exceed said sum.

(j). Denies the allegations contained in paragraph VII(j) of the answer, and particularly denies that the petitioner is liable as a transferee of the property of the taxpayer, Jennie Wolf, Deceased, and has become or is now answerable to the extent of the amount of the alleged deficiency in income tax, together with interest thereon or in or to any other amount or interest thereon.

### VIII.

Denies generally and specifically each and every material allegation contained in paragraphs

VII(a) to (j), inclusive, of respondent's answer, not hereinbefore especially admitted, qualified or denied.

Wherefore, the petitioner prays that the respondent's determination be disapproved, that the prayer in the answer be denied, and that the prayer in the petition be granted.

/s/ ROBT. T. JACOB,

Counsel for Petitioner.

State of Oregon,

County of Multnomah—ss.

Charlotte C. Cohon, being first duly sworn, says that she is the petitioner above named, that she has read the foregoing reply and is familiar with the statements contained therein, and that the statements contained therein are true, except those stated to be upon information and belief, and those she believes to be true.

/s/ CHARLOTTE C. COHON.

Subscribed and sworn to before me this 10th day of November, 1947.

[Seal] /s/ J. F. JOHNSON,

Notary Public for Oregon.

My Commission expires: 3/28/51.

[Lodged]: Nov. 19, 1947.

Filed Nov. 20, 1947, T.C.U.S.



[Title of Tax Court and Cause.]

MOTION FOR ORDER GRANTING  
PERMISSION TO AMEND PETITION

Comes now the petitioner the above entitled cause by Robt. T. Jacob, her counsel of record, and moves the Court for an order permitting him to amend her petition by adding to paragraph V of said petition immediately after sub-paragraph (a) or paragraph V a sub-paragraph to be designated (a.1) in form and substance as follows:

(a.1) During the year 1944 said Jennie Wolf instituted proceedings in the Tax Court of the United States against the Commissioner of Internal Revenue by filing in said court a petition, docket number 6263, appealing from a purported deficiency in income taxes for the calendar year 1941, in which petition said Jennie Wolf, as the petitioner therein, among other things, alleged:

“(a) Petitioner is a member of the partnership of Alaska Junk Company which said partnership is composed of four individuals, H. J. Wolf, Mrs. J. Wolf, S. Schnitzer and Mrs. R. Schnitzer, each owning a one-fourth interest therein.”

The Commissioner of Internal Revenue filed his answer to said petition in said court and in his answer admitted the above quoted allegation. Docket numbers 6262, 6264 and 6265 were similar proceedings instituted respectively by Harry J. Wolf, Sam Schnitzer and Rose Schnitzer, and in

the petitions in each of these dockets there was an allegation similar to the one above quoted, and in the answer to each said petition the Commissioner admitted said allegation. Thereafter the said proceeding docket number 6263, and the related dockets 6262, 6264 and 6265 were consolidated for trial and tried by the said Tax Court of the United States, and on or about the 23rd day of December, 1946, the said Tax Court of the United States made and entered findings of fact and its opinion, in which findings of fact the said court found:

“The petitioners are husbands and wives and members of a co-partnership, doing business under the firm name and style of Alaska Junk Company at Portland, Oregon. Each petitioner had a one-fourth interest in the firm. They filed individual income tax returns with the collector of internal revenue for the district of Oregon.

The partnership, Alaska Junk Company, was originally organized by petitioners, H. J. Wolf and S. Schnitzer, in 1911. Its business was the buying and selling of all sorts of salvage metals and materials. The original partnership continued until 1925 or 1926 when the wives of the partners, petitioners Jennie Wolf and Rose Schnitzer, were taken into the firm. That partnership is still in existence except that petitioner Jennie Wolf, the wife of H. J. Wolf, died in April, 1945.”

On or about the 24th day of September, 1946, the said Court entered its decisions in each of the said

causes and each of the said decisions, less formal parts, date, seal and signature, is as follows:

“Pursuant to the determination of the Court, as set forth in its Memorandum Findings of Fact and Opinion, entered Sept. 23, 1946, it is

Ordered and Decided: That there is no deficiency in income tax for the calendar year 1941.”

That the findings and decision in docket 6263 was a final adjudication in favor of said Jennie Wolf and against the Commissioner of Internal Revenue. The interest of Sam Schnitzer, Rose Schnitzer, Harry J. Wolf and Jennie Wolf in said Alaska Junk Company were exactly the same in the calendar years 1942 and 1943 as in the year 1941, and the fact that each of the said persons has said interests in said partnership during said years has become res judicata and the Respondent ought to be and is estopped to deny the same.

/s/ ROBT. T. JACOB,

Counsel for Petitioner.

Granted June 10, 1948.

/s/ LUTHER A. JOHNSON,

Judge.

Filed June 10, 1948, T.C.U.S.

[Title of Tax Court and Cause.]

ANSWER TO AMENDMENT TO PETITION

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for answer to the amendment to petition filed by the above-named petitioner admits and denies as follows:

V-(a.1). Admits the allegations contained in subparagraph (a.1) of paragraph V of the petition except those contained in the last two sentences thereof which are denied.

/s/ CHARLES OLIPHANT,  
Chief Counsel,  
Bureau of Internal  
Revenue.

Of Counsel:

B. H. NEBLETT,  
Division Counsel;

JOHN H. PIGG,  
LEONARD A. MARCUSSEN,  
Special Attorneys,  
Bureau of Internal Revenue.

Served July 29, 1948.

Received and Filed July 28, 1948, T.C.U.S.

The Tax Court of the United States  
Washington

Docket No. 14280

CHARLOTTE C. COHON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

### DECISION

Pursuant to Opinion of the Tax Court promulgated July 14, 1949, the respondent filed a computation on October 6, 1949, and the petitioner, on November 7, 1949, filed an acquiescence in the computation as filed by the respondent. Now, therefore, it is

Ordered and Decided: That there is a deficiency in income and victory tax due from this petitioner for the calendar year 1943 in the amount of \$42,273.99.

/s/ LUTHER A. JOHNSON,  
Judge.

Entered Nov. 9, 1949.

Served Nov. 10, 1949.



In the United States Court of Appeals  
for the Ninth Circuit

T. C. Docket No. 14280

CHARLOTTE C. COHON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

PETITION FOR REVIEW

Comes now the petitioner, by his attorneys of record, and respectfully shows this Honorable Court:

I.

The petitioner is an individual residing at 7825 S. E. Reed College Place, Portland, Oregon, and is one of three equal transferees of the residuary estate of Jennie Wolf, deceased. The return for the period here involved was filed by Jennie Wolf with the Collector of Internal Revenue for the District of Oregon.

II.

The respondent is the duly appointed, qualified and acting Commissioner of Internal Revenue of the United States and is hereinafter referred to as the "Commissioner."

III.

The taxes in controversy are income and victory taxes for the calendar year 1943.

## IV.

## Nature of Controversy

For many years prior to and during the taxable year before the court Sam Schnitzer, Harry J. Wolf, Rose Schnitzer and Jennie Wolf were doing business as copartners under the name and style of Alaska Junk Company. During the years 1942 and 1943 Alaska Junk Company was engaged in the business of buying, selling and generally dealing in junk, pipe, tools, machinery, hardware, scrap and other metals, and as a part of its regular business, made loans and advances to customers and affiliated enterprises, always treating these loans and advances as "accounts receivable" on its books of account.

Morris Schnitzer, a son of Sam Schnitzer, was engaged in a similar business and in 1941 organized the Oregon Electric Steel Rolling Mills (hereinafter referred to as "Oregon Steel") an Oregon corporation, to manufacture steel products. The company's authorized capital was 2,500 shares having a par value of \$100.00 each, a total capital of \$250,000.00. Upon final distribution of this stock the partners of Alaska Junk Company received 1,249 shares and Morris Schnitzer 625 shares.

From October, 1941, to November, 1943, Alaska Junk Company advanced to Oregon Steel, cash \$327,870.23, paid bills of \$166,340.16 and furnished goods at market prices to the amount of \$347,341.62, making a total of \$841,552.01.

All of these items were charged on Alaska Junk

Company's books as "accounts receivable" from Oregon Steel. On the books of Oregon Steel these items were entered as "accounts payable." Alaska Junk Company received payments of cash \$114,519.88, received stock of a par value \$124,900.00 and debenture notes of a face value of \$174,000.00, making total receipts of \$413,419.88, which items were credited to said accounts receivable.

Morris Schnitzer and Alaska Junk Company orally agreed that Morris Schnitzer would bear  $\frac{1}{3}$  of the total loss, if any, that might be sustained by Morris Schnitzer and Alaska Junk Company from advances to Oregon Steel over and above the advances credited to stock subscriptions. Alaska Junk Company in turn agreed to bear  $\frac{2}{3}$  of any such loss.

Alaska Junk Company was induced to make the advances, sell goods on credit and pay the bills of Oregon Steel upon a promise of early repayment, based upon engineering estimates of minimum earnings of \$50,000.00 per month and a production schedule to begin early in 1943.

In June, 1943, Morris Schnitzer was inducted into military service and Oregon Steel was unable to obtain competent management. As a result of this and other difficulties the operations were unsuccessful, and in November, 1943, ceased. It was then decided by the stockholders to withdraw from the enterprise, and Oregon Steel stock was then sold. Prior to the sale Oregon Steel issued Alaska Junk Company its promissory note for \$427,843.87, the balance of its account receivable, and issued its

note of \$26,829.28 to Schnitzer Steel Products Company (Morris Schnitzer). In exchange for these two notes Alaska Junk Company and Morris Schnitzer received a third mortgage note for \$151,000.00. This compromise resulted in a total loss of \$303,625.90 and by reason of the agreement between Morris Schnitzer and Alaska Junk Company, Alaska Junk Company sustained a loss of \$202,350.60, which was charged off as a bad debt.

On the partnership's return for 1943 a deduction of the \$202,350.60 was claimed as a bad debt. It is this amount which the Commissioner has disallowed as a deduction. The Commissioner's contention was upheld by the Tax Court of the United States and petitioner submits that in making its determination the Tax Court was in error.

## V.

The petitioner designates the following points on which he intends to rely on appeal to the United States Court of Appeals for the Ninth Circuit from the decision heretofore entered by the Tax Court of the United States:

1. The Tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the partnership in which petitioner's transferror was a partner was not deductible as a bad debt in computing net income subject to taxation.

2. The Tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the partnership in which petitioner's transferror was a partner was not a bad debt.



3. The Tax Court erred in holding that all of the advances, including said sum of \$202,350.60, of the partnership in which petitioner's transferror was a partner were contributions to capital.

4. The Tax Court erred in not finding and holding that all of said sum of \$202,350.60 was a loan made by the partnership in which petitioner's transferror was a partner.

5. The decision entered by the Tax Court herein is not supported by the evidence, is contrary to the evidence and is in disregard of it.

6. The Tax Court erred in determining that there was a deficiency in income and victory taxes for the calendar year 1943 due from the above-named petitioner.

Wherefore, the petitioner petitions that the decision of the Tax Court of the United States be reviewed by the United States Court of Appeals for the Ninth Circuit; that a copy of the record on review be prepared in accordance with law and with the rules of said Court and transmitted to the Clerk of said Court for filing and that appropriate action be taken by said Court to review and correct the decision of the Tax Court which petitioner submits is erroneous.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,

Attorneys for Petitioner.

Received and Filed Jan. 4, 1950, T.C.U.S.



In the United States Court of Appeals  
for the Ninth Circuit

T. C. Docket No. 14280

CHARLOTTE C. COHON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

NOTICE OF FILING OF PETITION  
FOR REVIEW

To: Charles Oliphant, Chief Counsel for the Bureau of Internal Revenue.

You will please take notice that on the 4th day of January, 1950, the petitioner above named filed with the Clerk of the Tax Court of the United States at Washington, D. C., a Petition for Review by the United States Court of Appeals for the Ninth Circuit of the decision of the Tax Court of the United States heretofore entered in the above-entitled proceeding.

A copy of said Petition for Review as filed is attached hereto and served upon you.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES.

Receipt of Copy acknowledged.

Received and Filed Jan. 9, 1950, T.C.U.S.

The Tax Court of the United States  
Washington

[Title of Cause.]

CERTIFICATE

I, Victor S. Mersch, Clerk of The Tax Court of the United States, do hereby certify that the foregoing documents, 1 to 13, inclusive, constitute and are all of the original papers and proceedings before The Tax Court of the United States as set forth in the "Designation of Record" except the original exhibits 1-27, incl., 28, 30, 31, 33-36, incl., 65, 66, 72-79, incl.; A-Z, AA-HH, incl., on file in my office as the original record in the proceeding and in which the petitioner in The Tax Court proceeding has initiated an appeal as above numbered and entitled, together with a true copy of the docket entries in said Tax Court proceeding, as the same appear in the official docket book in my office.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia, this 23rd day of January, 1950.

[Seal]      /s/ VICTOR S. MERSCH,  
Clerk.

[Endorsed]: No. 12475. United States Court of Appeals for the Ninth Circuit. Charlotte C. Cohon, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Petition to Review a Decision of The Tax Court of the United States.

Filed February 7, 1950.

/s/ PAUL P. O'BRIEN,  
Clerk of the United States Court of Appeals for  
the Ninth Circuit.

**In the United States Court of Appeals  
for the Ninth Circuit**

**T. C. Docket No. 14208**

**SAM SCHNITZER,**

**Petitioner,**

**vs.**

**COMMISSIONER OF INTERNAL REVENUE,  
Respondent.**

**T. C. Docket No. 14209**

**ESTATE OF HARRY J. WOLF, Deceased, by  
MONTE L. WOLF, Administrator de bonis  
non with the will annexed of said Estate,  
Petitioner,**

**vs.**

**COMMISSIONER OF INTERNAL REVENUE,  
Respondent.**

**T. C. Docket No. 14278**

**MONTE L. WOLF,**

**Petitioner,**

**vs.**

**COMMISSIONER OF INTERNAL REVENUE,  
Respondent.**

T. C. Docket No. 14279

BLOSSOM M. GOLDSTEIN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14280

CHARLOTTE C. COHON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14372

ESTATE OF JENNIE WOLF, Deceased, by

MONTE L. WOLF, Administrator de bonis

non with the will annexed of said Estate,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

## MOTION TO CONSOLIDATE APPEALS

The above named petitioners on review and each of them, acting by and through their attorneys of record, hereby move this court to consolidate the above entitled proceedings for purposes of the printed record on appeal, the briefing, the hearing,



the argument, the decision and for all other purposes connected with the final disposition of said proceedings on review.

This motion is based on the grounds that all of the above entitled proceedings were consolidated for trial below in the Tax Court, that the Tax Court made but one set of findings of fact and rendered but one opinion in connection with all of these cases, that each of these cases involves the same facts, that each of the petitioners on review was either a partner or is now the transferee of a decedent who was a partner in a partnership known as the Alaska Junk Company, that the sole question for decision concerns the deductibility of a bad debt by said Alaska Junk Company, and that the decision on this single point is determinative of the income tax liability of each of said partners or said transferees of partners who are the petitioners herein.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,

917 Public Service Building,  
Portland 4, Oregon.

I, Randall S. Jones, being on oath first duly sworn, depose and say:

That on the 13th day of February, 1950, I served the foregoing Motion to Consolidate Appeals upon Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, by on said day depositing a duly certified copy thereof in the United

States mails with full postage and registration charges prepaid, addressed to Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, Internal Revenue Building, Washington, D. C. Said papers were deposited in the United States mails at the Federal Post Office, S. W. Sixth and Main Streets, Portland 4, Oregon.

/s/ RANDALL S. JONES.

Subscribed and sworn to before me this 13th day of February, 1950.

[Seal] /s/ JACQUELINE MOHLAND,  
Notary Public for Oregon.

My commission expires: 9-22-52.

So Ordered:

/s/ WILLIAM DENMAN,  
Chief Judge.

/s/ HOMER BONE,

/s/ WM. E. ORR,

U. S. Circuit Judge.

[Endorsed]: Filed Feb. 15, 1950.

[Title of Court of Appeals and Causes.]

STATEMENT OF POINTS ON WHICH  
PETITIONERS INTEND TO RELY

The petitioners on review hereby enumerate the points on which they intend to rely on appeal and which are as follows:

1. The Tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the partnership in which petitioners were partners was not a bad debt and not deductible in computing the net income of said partnership and petitioners' net income subject to taxation for the taxable year 1943.

2. The Tax Court erred in holding that the total, or any amount in excess of \$125,000.00, representing bills paid for, cash advanced to, and goods sold to Oregon Electric Steel Rolling Mills by the partnership in which petitioners or their transferrors were partners, constituted a contribution to the capital of said Oregon Electric Steel Rolling Mills.

3. The Tax Court erred in not finding and holding that all and every part of said sum of \$202,350.60 was a debt owed to the partnership in which petitioners were partners.

4. The decision entered by the Tax Court herein is contrary to the law, the Tax Court's findings of fact, and the evidence; and is not supported by said findings of fact or the evidence and is in disregard of both said findings of fact and the evidence.

5. The Tax Court erred in failing to include in its findings material facts clearly established by the evidence which further show that the bills paid, cash advanced and goods sold to Oregon Electric Steel Rolling Mills constituted an indebtedness owed to the partnership.

6. The Tax Court erred in admitting respondent's exhibits O, P, Q, U, V, AA, FF, GG and HH over objections of petitioner for the reasons set forth respectively on pages 120, 121, 122, 129, 134, 137, 495, 589-591, 621 and 636, 639 and 640 of the *Report's* Transcript of the Proceedings before said court.

7. The Tax Court erred in receiving oral testimony adduced by respondent over objections of the petitioners as set forth in those portions from the Reporter's Transcript of the Proceedings before said court which the petitioners have designated for inclusion in the Printed Record.

8. The Tax Court erred in sustaining objections of the respondent to questions asked by petitioners and to oral testimony offered by petitioners, which questions, objections and rulings thereon are set forth in those portions from the Reporter's Transcript of the Proceedings before said court which



the petitioners have designated for inclusion in the Printed Record.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,  
917 Public Service Bldg.,  
Portland 4, Oregon.

I, Randall S. Jones, being on oath first duly sworn, depose and say:

That on the 13th day of February, 1950, I served the Statement of Points on which Petitioners Intend to Rely upon Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, by on said day depositing a duly certified copy thereof in the United States mails with full postage and registration charges prepaid, addressed to Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, Internal Revenue Building, Washington, D. C. Said papers were deposited in the United States mails at the Federal Post Office, S. W. Sixth and Main Streets, Portland 4, Oregon.

/s/ RANDALL S. JONES.

Subscribed and sworn to before me this 13th day of February, 1950.

[Seal] /s/ JACQUELINE MOHLAND,  
Notary Public for Oregon.

My commission expires: 9-22-52.

[Endorsed]: Filed Feb. 15, 1950.





No. 12476

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United States  
Court of Appeals  
For the Ninth Circuit.

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ESTATE OF JENNIE WOLF, Deceased, by Monte  
L. Wolf, Administrator de bonis non with the  
will annexed of said Estate,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

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Transcript of Record

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Petition to Review a Decision of the Tax Court  
of the United States

FILED

APR 1 1931

PAUL P. O'BRIEN,

CLERK



No. 12476

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United States  
Court of Appeals  
For the Ninth Circuit.

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ESTATE OF JENNIE WOLF, Deceased, by Monte  
L. Wolf, Administrator de bonis non with the  
will annexed of said Estate,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

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Transcript of Record

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Petition to Review a Decision of the Tax Court  
of the United States





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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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## NAMES AND ADDRESSES OF ATTORNEYS

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Special Attorneys,

Bureau of Internal Revenue.

## The Tax Court of the United States

T. C. Docket No. 14372

ESTATE OF JENNIE WOLF, Deceased, by  
Harry J. Wolf, Administrator de bonis non of  
said estate with will annexed, and by Harry J.  
Wolf, former executor of said estate,  
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

## PETITION

The above named petitioner hereby petitions the above entitled Court for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his Notice of Deficiency, (Bureau Symbols IT:90:D:DLA) dated March 3, 1947, and as a basis of this proceeding alleges as follows:

## I.

The petitioner is the duly appointed, qualified and acting Administrator de bonis non of the Estate of Jennie Wolf, Deceased, with will annexed, and he is the former Executor of said estate. He resides at 3111 S. E. Lambert Street, Portland, Oregon, and has his place of business at 900 S. W. First Avenue, Portland, Oregon. The returns for the periods here involved were filed by Jennie Wolf with the Collector for District of Oregon.

## II.

The Notice of Deficiency (a copy of which is attached and marked Exhibit A) was mailed to the petitioner from Seattle, Washington, under date of March 3, 1947, and was addressed to him as follows:

Estate of Jennie Wolf, Deceased  
Mr. Harry J. Wolf, Executor  
900 S. W. First Avenue  
Portland, Oregon

## III.

The taxes in controversy are income taxes for the calendar years 1942 and 1943, and the amount in controversy does not exceed \$42,273.99, which sum is equal to the amount of deficiency asserted. The petitioner contends that at all times during the calendar years 1942 and 1943, Jennie Wolf was a partner in The Alaska Junk Company with an interest therein equal to that of her husband, Harry J. Wolf, who is the same individual as the petitioner herein. Said partnership interest of Jennie Wolf is in issue before this Court in the appeal hereinafter mentioned, and in the event this Court in said appeal should determine that Jennie Wolf was not such partner during said calendar years, the petitioner claims that said Estate of Jennie Wolf, Deceased, is entitled to a refund of \$36,950.97 for said calendar years and that such amount was paid by said Jennie Wolf within three years of the mailing of said Notice of Deficiency as income and



victory taxes on account of her distributive share of the net income of said partnership for said calendar years, or in such event and if said estate is not legally entitled to receive such refund that the three residuary legatees named in the will of said Jennie Wolf, Deceased, are each entitled to a refund of \$12,316.99 which is one-third of said amount of \$36,950.97.

#### IV.

The determination of the tax set forth in said Notice of Deficiency is based upon the following errors:

(a) The Commissioner erred in disallowing as a deduction of The Alaska Junk Company in the calendar year 1943 the sum of \$202,350.60 as (1) a bad debt owed to The Alaska Junk Company by the Oregon Electric Steel Rolling Mills which became worthless in said calendar year, or (2) as a loss deductible under the provisions of Sec. 23 (e), I.R.C.

(b) The Commissioner erred in including an additional \$50,587.65 in the Income Tax Net Income and Victory Tax Net Income of said Jennie Wolf for the calendar year 1943 as a result of his said disallowance of the said sum of \$202,350.60 as a deduction of The Alaska Junk Company for said calendar year.

#### V.

The facts upon which the petitioner relies as the basis of this proceeding are as follows:

**Re Bad Debt Loss**

(a) At and during the calendar years 1942 and 1943, and for a great many years prior thereto, Sam Schnitzer, Rose Schnitzer, Harry J. Wolf and said Jennie Wolf were co-partners under the names and styles of The Alaska Junk Company and Schnitzer-Wolf Machinery Company, and as such co-partners were engaged in the business of buying, selling and generally dealing in junk, new and second hand pipe, tools, machinery, hardware, metal and metal products of every character, and in promoting and financing business enterprises of a nature related to the other said activities of said partnership, and the principal place of business of said partners was in Portland, Oregon. During all said times each of the said persons owned a one-quarter interest in the business and property of said partnership, which said partnership is hereinafter referred to as The Alaska Junk Company.

(b) At and during all the times hereinafter mentioned the Oregon Electric Steel Rolling Mills, hereinafter called the corporation, was a corporation having an authorized capital stock of 2,500 shares consisting of common stock of a par value of \$100.00 each. Sam Schnitzer and Harry J. Wolf each subscribed to a portion of the capital stock, which portion was subsequently issued and thereupon immediately reissued so as to divide it equally among said four partners. Thereafter additional stock was issued in substantially equal amounts to

each of the four partners. Said corporation was fully paid for all said stock. The balance of the issued stock of said corporation was owned by other persons. Morris Schnitzer, son of Sam Schnitzer and Rose Schnitzer, owned all of the said balance except three shares.

(c) Said Morris Schnitzer at and during all times hereinafter mentioned was engaged in Portland, Oregon in the business of buying and selling new and used iron, steel, tools and machinery and conducted such business under the name and style of the Schnitzer Steel Products Co.

(d) In the course of its business The Alaska Junk Company between October 22, 1941 and November 22, 1943, on an open account, at the instance and request of said corporation, advanced money to said corporation, either directly or by making payments on its account to its creditors, purchased and furnished it with merchandise charging the cost thereof to it, and sold goods, wares and merchandise to it at the regular prices charged by The Alaska Junk Company to the trade in general. On November 26, 1943 the balance due and owing to The Alaska Junk Company from said corporation on said open account was \$428,132.13.

(e) In consideration of said open account being credited with the sum of \$174,000.00 the said corporation made, executed and delivered to The Alaska Junk Company one hundred seventy-four (174) First Debentures (unsecured) in the total

amount of \$174,000.00, bearing interest at 8% per annum, and on July 14, 1943 said Alaska Junk Company credited said open account with said amount of \$174,000.00, and charged its "Stocks and Bonds" account with a like sum. For a valuable consideration seventy-five (75) such debentures in the sum of \$75,000.00 were also executed and delivered by said corporation to Morris Schnitzer. No payments of either principal or interest were ever made on any of said debentures.

(f) Soon after the organization of said corporation, The Alaska Junk Company and Morris Schnitzer entered into a contract of guaranty whereby it was agreed that in the event a loss should be sustained by The Alaska Junk Company as a result of its extending credit to said corporation, Morris Schnitzer would pay to The Alaska Junk Company so much of any such loss as should exceed two-thirds of the total combined losses of himself and The Alaska Junk Company sustained on account of the extension of credit to said corporation by himself and The Alaska Junk Company, and a corresponding guaranty was made by The Alaska Junk Company to Morris Schnitzer to the extent of one-third of the total combined losses of said parties sustained through the extension of credit to said corporation.

(g) The idea for the establishment of said corporation was conceived by Morris Schnitzer and from its inception to July 17, 1943 he acted as its



president and manager. On said date he was inducted into the armed service of the United States and this left the corporation without a directing head sufficiently informed and capable of carrying out the purposes of the corporation. Extended and repeated efforts were made to secure a suitable manager to take his place. None could be found. None of the remaining stockholders of said corporation or partners of The Alaska Junk Company were able to properly manage the plant. Its operation bogged down. There was a \$678,843.70 mortgage against its real estate. It owed \$149,650.00 for which its inventories were security, and in addition to the sums it owed The Alaska Junk Company and Morris Schnitzer, it owed \$190,684.06 on open accounts. It lost money, became unable to pay its debts, and it became apparent that it would be impossible for it to carry on and operate profitably. Thereupon many industrialists of large financial ability were solicited in repeated efforts to find some person or organization that would take over the interests of The Alaska Junk Company and Morris Schnitzer in said corporation under such terms as would save them from loss, or at least, under terms that would result in as little loss to them as possible. Including those solicited were Kenneth E. Hall and A. M. Mears, then of the Hesse-Ersted Iron Works. After extended negotiations an agreement was made by and between said Hall, Mears, The Alaska Junk Company, and Morris Schnitzer, by his attorney-in-fact, Sam



Schnitzer, whereby said Hall and Mears agreed to purchase the outstanding stock of said corporation at a nominal sum and thereafter to cause said corporation to execute and deliver a promissory note to The Alaska Junk Company and Morris Schnitzer in the sum of \$249,000.00 to be secured by a second mortgage upon its properties in payment of all said debentures, and to execute and deliver a promissory note to said persons in the sum of \$151,000.00 secured by a third mortgage upon said properties in compromise and full payment of the balance due on said open account and in complete satisfaction of a debt of \$26,493.77 then due and owing from said corporation to Morris Schnitzer. The Alaska Junk Company entered into said agreement for the reason that it gave The Alaska Junk Company the best opportunity it could find to realize the greatest possible amount on the obligations owed to it by said corporation.

(h) As evidence of the correct balance due The Alaska Junk Company on its said open account a demand promissory note in the amount of said balance was executed and delivered by said corporation to The Alaska Junk Company, and as evidence of the correct amount of said debt owed by said corporation to Morris Schnitzer a demand promissory note in the amount of said debt was executed and delivered by said corporation to Sam Schnitzer, the attorney-in-fact for Morris Schnitzer.

(i) On November 26, 1943, subsequent to the execution and delivery of the demand notes mentioned in paragraph V (h), all of the issued stock of said corporation was sold to said Hall and Mears and transferred to them or their order pursuant to the agreement mentioned in paragraph V (g); and thereafter said corporation executed and delivered promissory notes and a second and a third mortgage, and the same were accepted by The Alaska Junk Company and Morris Schnitzer, by his said attorney-in-fact, all in accordance with said agreement.

(j) Upon the receipt of said promissory note and second mortgage for the amount of \$249,000.00 all of the said debentures were returned to said corporation as fully paid and satisfied, and The Alaska Junk Company credited its said open account with \$142,200.33, which was its pro-rata share of the said promissory note and third mortgage for \$151,000.00, and pursuant to said guaranty agreement charged Morris Schnitzer with \$83,581.20 and credited said open account with an equal amount, thereby reducing the balance of said open account to \$202,350.60, which balance became worthless within the calendar year 1943, because under the terms of the settlement with said corporation embodied in the agreement mentioned in paragraph V (g) no further amount could be realized on said unpaid balance from the corporation, and the said sum of \$83,581.20 was the entire amount for which

Morris Schnitzer was liable under the said guaranty. On December 31, 1943 The Alaska Junk Company charged off the said balance as a bad debt, and nothing has since been received thereon.

(k) On account of the matters and things hereinabove stated The Alaska Junk Company sustained a bad debt or business loss in the calendar year 1943 in the sum of \$202,350.60.

(l) The Commissioner arbitrarily considered that the said unpaid and worthless balance of \$202,350.60 represented a contribution by The Alaska Junk Company to the capital of said corporation. Petitioner is informed, believes and therefore alleges that there was no intention at any time by any of the said partners that the said amount, or any portion thereof, should be a capital contribution to said corporation, but on the contrary it was the intention of The Alaska Junk Company that it was extending credit and that the full balance shown by its said open account would be repaid to it by said corporation.

### Re Refund

(m) Said Jennie Wolf was the wife of said Harry J. Wolf and the mother of Charlotte C. Cohon, Blossom M. Goldstein and Monte L. Wolf. Jennie Wolf died on April 8, 1945, and left a will which was duly admitted to probate by an order of the Circuit Court of the State of Oregon for the County of Multnomah, Probate Department, made and entered on April 18, 1945, in the Matter of

Estate of Jennie Wolf, Deceased, Probate No. 53880. By the terms of said will said Jennie Wolf directed that her funeral expenses, just debts, estate and inheritance taxes be paid, bequeathed specific articles of jewelry, household furniture, fixtures, linens, silverware, and certain specified sums of money, and then disposed of all the rest, residue and remainder of her property and estate pursuant to the eighth paragraph of said will. The second and eighth paragraphs of said will read as follows:

“Second: I have a husband named Harry J. Wolf. I have three living children, whose names and the date of their births are as follows, to wit: (1) Monte L. Wolf, who was born on April 5, 1909; and (2) Charlotte C. Cohon—nee Wolf, who was born on September 8, 1911; and (3) Blossom M. Goldstein—nee Wolf, who was born on July 8, 1919.”

“Eighth: I give and bequeath and devise all of the rest, residue and remainder of my property and estate—real and personal and mixed, and wheresoever situated and whether acquired before or after making this Will—in equal shares to my above named three children.”

There was no person named in said will as a child of Jennie Wolf other than those named in said second paragraph, and she had no other children.

(n) Said Harry J. Wolf, was duly appointed the executor of said will and estate, qualified as such, and administered the estate. He filed his final



account, which was duly approved and distribution was ordered by said Court on March 29, 1946. Distribution was thereupon made of all the property and estate of said Jennie Wolf, Deceased, that remained in the hands of said executor, and by order of said Court duly made, entered and effective on April 1, 1946, the administration of said estate was fully and completely closed and Harry J. Wolf was discharged and released as executor of said estate. There was no executor of said will or estate or personal representative of said Jennie Wolf, Deceased, since the date last mentioned until the 28th of May, 1946, that on said date this petitioner, Harry J. Wolf, was duly and regularly appointed the Administrator de bonis non of the Estate of Jennie Wolf, Deceased, with will annexed by the said Circuit Court of the State of Oregon for the County of Multnomah, Probate Department, said probate proceeding No. 53880, that he has qualified and is now the acting Administrator de bonis non of said estate, and has been duly authorized to institute this appeal.

(o) The Commissioner in determining the taxable income of said Harry J. Wolf for the calendar years 1942 and 1943 refused to recognize that Jennie Wolf was a partner during said calendar years in the said business carried on under the name of The Alaska Junk Company with an interest therein equal to that of Harry J. Wolf, although the Commissioner had recognized her as such partner for many years prior thereto, and that based



on his said refusal to recognize her as such partner during said years he treated her distributive share of the net profits of said partnership for said years as income of Harry J. Wolf and determined a deficiency in the income tax liability of said Harry J. Wolf for said calendar years in the sum of \$151,049.05, and that said Harry J. Wolf has filed with the Clerk of this Court, or at least, has mailed to him for filing, an appeal to this Court wherein said Harry J. Wolf alleged that Jennie Wolf was a partner, with such interest, during said calendar years and that the Commissioner erred in refusing to recognize her as such.

(p) In the event the issue referred to in paragraph V (o) should be determined by this Court adversely to said contentions of said Harry J. Wolf, the said Jennie Wolf will have overpaid her income and victory taxes for said calendar years by the sum of \$36,950.97.

(q) All of the specific and pecuniary bequests made by said Jennie Wolf in her said will were paid in full, and the entire amount of said sum of \$36,950.97 was paid on said income and victory taxes in diminution of the interests of Charlotte C. Cohon, Blossom M. Goldstein, and Monte L. Wolf as the residuary legatees under said will of said Jennie Wolf, Deceased.

(r) None of the foregoing allegations are in any way intended as an admission that the Commissioner was correct in his refusal to recognize said

partnership interest of Jennie Wolf, and paragraphs (m) through (q) are included herein only to protect the interests of said estate and of said residuary legatees in the event this Court should determine said partnership issue in said appeal adversely to the interests of Harry J. Wolf.

Wherefore, petitioner prays that this Court may hear this proceeding and determine that Jennie Wolf paid her taxes in full for all years in question and that there is no deficiency in her income and/or victory taxes due from her estate for said years, and petitioner further prays that this cause not be determined by this Court prior to its determination of said partnership issue in said appeal of Harry J. Wolf, and if said issue is determined adversely to the interests and contentions of said Harry J. Wolf, then and in such event, that this Court determine that Jennie Wolf made an overpayment of her income and victory taxes for the calendar years in question in the sum of \$36,950.97, and that she paid the same within three years prior to the mailing of said Notice of Deficiency, and petitioner also prays for such further relief as may be just and proper in the premises.

/s/ ROBT. T. JACOB,

Counsel for Petitioner.

State of Oregon,  
County of Multnomah—ss.

Harry J. Wolf, being first duly sworn, says that he is the duly appointed, qualified and acting Administrator de bonis non of the above Estate of Jennie Wolf, Deceased, and the former Executor of said estate, and as such Administrator de bonis non is duly authorized to verify the foregoing petition for and in behalf of said estate, that he has had the said petition read to him, and is familiar with the statements contained therein, and that the statements contained therein are true.

/s/ HARRY J. WOLF.

Subscribed and sworn to before me this 28th day of May, 1947.

[Seal]      /s/ J. F. JOHNSON,  
Notary Public for Oregon.

My Commission expires: March 28, 1951.

EXHIBIT A

Treasury Department  
Internal Revenue Service  
Seattle 1, Washington

March 3, 1947.

Office of Internal Revenue Agent in Charge Seattle  
Division, 305A 1331 Third Avenue Building

IT:90D:DLA

Estate of Jennie Wolf, Deceased  
Mr. Harry J. Wolf, Executor  
900 S. W. First Avenue  
Portland, Oregon

Dear Mr. Wolf:

You are advised that the determination of the income tax liability of Jennie Wolf, deceased, for the taxable year ended December 31, 1943, discloses a deficiency of \$42,273.99 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days (not counting Saturday, Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with The Tax Court of the United States, at its principal address, Washington 25, D. C., for a redetermination of the deficiency or deficiencies.

Should you not desire to file a petition, you are re-

requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, Seattle 1, Washington, for the attention of IT:90D:DLA. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency or deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Very truly yours,

JOSEPH D. NUNAN, JR.,

Commissioner.

By /s/ S. R. STOCKTON,

Internal Revenue Agent in  
Charge.

DLA:mts

Enclosures

Statement

Form of waiver



## Statement

IT:90D:DLA

Estate of Jennie Wolf, Deceased  
 Mr. Harry J. Wolf, executor  
 900 S. W. First Avenue  
 Portland, Oregon

Tax liability for the taxable year ended December 31, 1943.

Income Tax .....	Deficiency
	\$ 42,273.99

In making this determination of your income tax liability, careful consideration has been given to the report of examination dated June 3, 1946, to your protest dated October 23, 1946, and to the statements made at the conference held on January 22, 1947.

## Taxable Year Ended December 31, 1943

## Adjustments to Net Income

	Income Tax Net Income	Victory Tax Net Income
Net income as disclosed by return .....	\$ 52,654.75	\$ 56,514.91
Unallowable deductions and additional income:		
(a) Income from partnership .....	50,587.65	50,587.65
Net income adjusted .....	\$103,242.40	\$107,102.56

## Explanation of Adjustments

(a) It is held after examination of the 1943 return filed by the partnership, Alaska Junk Co., that your distributive share of the income from that partnership was \$107,101.58. Reported on the return, \$56,513.93. Additional income from partnership, \$50,587.65.

## Computation of Income and Victory Tax

Income tax net income, adjusted .....	\$103,242.40
Less: Personal exemption .....	None
Surtax net income .....	\$103,242.40
Less: Earned income credit.....	300.00
Balance subject to normal tax .....	\$102,942.40
Normal tax at 6 percent on \$102,942.40..\$	6,176.54
Surtax on \$103,242.40 .....	61,701.50
Total income tax .....	\$ 67,878.04
Victory tax net income adjusted .....	\$107,102.56
Less: Specific exemption .....	624.00
Income subject to victory tax .....	\$106,478.56
Victory tax before credit, 5% of \$106,478.56 .....	\$ 5,323.93
Less: Victory tax credit .....	500.00
Net victory tax .....	\$ 4,823.93
Net income tax and victory tax .....	\$ 72,701.97
Income tax for 1942 .....	\$ 26,091.94
Amount of net income tax and victory tax .....	\$ 72,701.97
Forgiveness feature:	
(a) Amount of income tax for 1942....\$	26,091.94
(b) Amount forgiven, $\frac{3}{4}$ of \$26,091.94 .....	19,568.95
(c) Amount unforgiven .....	\$ 6,522.99
Total income and victory tax liability .....	\$ 79,224.96
Income and victory tax liability disclosed by return, Account No. 353534 .....	\$ 36,950.97
Deficiency of income tax .....	\$ 42,273.99

Received and filed June 2, 1947, T.C.U.S.

[Title of Tax Court and Cause.]

### ANSWER

Comes Now the Commissioner of Internal Revenue, by his attorney, Charles Oliphant, Acting Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed herein, admits, denies and alleges as follows:

I. Admits the allegations contained in paragraph I of the petition.

II. Admits the allegations contained in paragraph II of the petition.

III. Admits that the taxes in controversy are, in part, income taxes for the calendar years 1942 and 1943, and that the alleged partnership interest of the decedent, Jennie Wolf, in the business carried on under the name of the Alaska Junk Company during the years 1942 and 1943 is in issue before this Court. For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth or falsity thereof, denies that the surviving spouse of the decedent, Harry J. Wolf, is the same individual as the petitioner herein. Denies the remaining allegations of fact contained in paragraph III of the petition, but admits that petitioner makes the contentions as set forth in said paragraph. Alleges that the income tax liability of the decedent, Jennie Wolf, for the year 1942, is involved in this proceeding only by reason of the forgiveness feature of section 6 of the Current Tax Payment Act of 1943; that no part of the de-

iciency in income and victory tax as determined by respondent in this proceeding, in the amount of, to wit: \$42,273.99, arises out of or is attributable to any adjustment made by respondent to or in respect of the net income as reported by decedent for the taxable year 1942, and that the alleged partnership interest of the decedent, Jennie Wolf, in the business carried on under the name of Alaska Junk Company during the years 1942 and 1943 is in issue before this Court in the related proceedings entitled Harry J. Wolf, Docket No. 14209, and Sam Schnitzer, Docket No. 14208; also in the related transferee proceedings entitled Monte L. Wolf, Docket No. 14278; Blossom M. Goldstein, Docket No. 14279; and Charlotte C. Cohon, Docket No. 14280.

IV(a) and (b). Denies that he erred in his determination of the deficiency shown by the notice of deficiency from which petitioner's appeal is taken. Specifically denies that he erred in the manner and form as alleged in paragraph IV(a) and (b) of the petition.

V(a). Denies the allegations contained in paragraph V(a) of the petition, except to the extent that in the event the decisions of this Court in the pending related cases of Harry J. Wolf, Docket No. 14209, and Sam Schnitzer, Docket No. 14208, should be adverse to respondent, i.e., the Court's decisions in those cases should be predicated upon a finding and holding by said Court that the decedent, Jennie Wolf, was, during the taxable years 1942 and 1943, a valid and bona fide partnership in the busi-

ness known and carried on under the name of Alaska Junk Company, and said decisions shall have become final, then and in that event, and upon that condition only, the respondent admits the allegations contained in said paragraph V(a) of the petition.

(b) to (j), inclusive. For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth or falsity thereof, denies the allegations contained in paragraph V(b) to (j), inclusive, of the petition.

(k). Denies the allegations contained in paragraph V(k) of the petition.

(l) Admits that he, the Commissioner, considered the balance of \$202,350.60 as a capital investment. Denies the remaining allegations contained in paragraph V (l) of the petition.

(m) and (n). Admits the allegations contained in paragraph V(m) and (n) of the petition.

(o). Admits that he, the Commissioner, in determining the taxable income of Harry J. Wolf for the calendar years 1942 and 1943, refused to recognize that Jennie Wolf was a partner during said calendar years in the business carried on under the name of Alaska Junk Company with an interest therein equal to that of Harry J. Wolf; that based on his said refusal to recognize the decedent, Jennie Wolf, as such partner during said years, he treated her alleged distributive share of net profits in said busi-



ness for said years as income of Harry J. Wolf and determined a deficiency in income and victory tax liability of said Harry J. Wolf for the year 1943 in the amount of, to wit: \$151,049.05; and that said Harry J. Wolf has filed with this Court his petition, at Docket No. 14209, as aforesaid, wherein he alleged that the decedent, Jennie Wolf, was a partner, with such interest, during said calendar years, and that the Commissioner erred in refusing to recognize her as such. Denies the remaining allegations contained in paragraph V(o) of the petition. Alleges that the determination as made by him, the Commissioner, in this proceeding, and the mailing of the notice of deficiency as alleged in paragraph II of the petition herein, though inconsistent with the determination as made by him, the Commissioner, in the proceeding entitled Harry J. Wolf, Docket No. 14209, now pending before the Court, as aforesaid, was and is necessary and appropriate in order to fully protect the revenue and the interests of the United States.

(p). Admits that in the event the issue referred to in paragraph V(o) of the petition, which said issue is presented in the pending proceeding entitled Harry J. Wolf, Docket No. 14209, as aforesaid, should be determined by this Court adversely to the contentions of said Harry J. Wolf, the decedent, the said Jennie Wolf, will have overpaid her income and victory tax for the year 1943. For lack of sufficient information or knowledge upon the basis of which to form a belief as to the truth or

falsity thereof, denies the remaining allegations contained in paragraph V(p) of the petition.

(q). Admits that all the specific and pecuniary bequests made by the decedent, the said Jennie Wolf, in her said will, were paid in full. Denies the remaining allegations contained in paragraph V(q) of the petition.

(r). Because of the absence of any allegation of fact therein, respondent neither admits nor denies the statements set forth in paragraph V(r) of the petition.

VI. Denies generally and specifically each and every material allegation contained in the petition, not hereinbefore specifically admitted, qualified, or denied.

Wherefore, it is prayed that the petitioner's appeal be denied and that the Commissioner's determination of deficiency be approved.

/s/ CHARLES OLIPHANT, JHP  
Acting Chief Counsel, Bureau  
of Internal Revenue.

Of Counsel:

B. H. NEBLETT,  
Division Counsel.

JOHN H. PIGG,

R. G. HARLESS,

Special Attorneys,

Bureau of Internal Revenue.

Received and filed Aug. 7, 1947, T.C.U.S.

[Title of Tax Court and Cause.]

MOTION FOR ORDER GRANTING  
PERMISSION TO AMEND PETITION

Comes now the petitioner in the above entitled cause by Robt. T. Jacob, the counsel of record, and moves the Court for an order permitting him to amend the petition by adding to paragraph V of said petition immediately after sub-paragraph (a) of paragraph V a sub-paragraph to be designated (a.1) in form and substance as follows:

(a.1) During the year 1944 said Jennie Wolf instituted proceedings in the Tax Court of the United States against the Commissioner of Internal Revenue by filing in said court a petition, docket number 6263, appealing from a purported deficiency in income taxes for the calendar year 1941, in which petition said Jennie Wolf, as the petitioner therein, among other things, alleged:

“(a) Petitioner is a member of the partnership of Alaska Junk Company, which said partnership is composed of four individuals, H. J. Wolf, Mrs. J. Wolf, S. Schnitzer and Mrs. R. Schnitzer, each owning a one-fourth interest therein.”

The Commissioner of Internal Revenue filed his answer to said petition in said court and in his answer admitted the above quoted allegation. Docket number 6262, 6264 and 6265 were similar proceedings instituted respectively by Harry J.

Wolf, Sam Schnitzer and Rose Schnitzer, and in the petitions in each of these dockets there was an allegation similar to the one above quoted, and in the answer to each said petition the Commissioner admitted said allegation. Thereafter the said proceeding docket number 6263, and the related dockets 6262, 6264 and 6265 were consolidated for trial and tried by the said Tax Court of the United States, and on or about the 23rd day of December, 1946, the said Tax Court of the United States made and entered findings of fact and its opinion, in which findings of fact the said court found:

“The petitioners are husbands and wives and members of a co-partnership, doing business under the firm name and style of Alaska Junk Company at Portland, Oregon. Each petitioner had a one-fourth interest in the firm. They filed individual income tax returns with the collector of internal revenue for the district of Oregon.

The partnership, Alaska Junk Company, was originally organized by petitioners, H. J. Wolf and S. Schnitzer, in 1911. Its business was the buying and selling of all sorts of salvage metals and materials. The original partnership continued until 1925 or 1926 when the wives of the partners, petitioners Jennie Wolf and Rose Schnitzer, were taken into the firm. That partnership is still in existence except that petitioner Jennie Wolf, the wife of H. J. Wolf, died in April, 1945.”



On or about the 24th day of September, 1946, the said Court entered its decisions in each of the said causes and each of the said decisions, less formal parts, date, seal and signature, is as follows:

“Pursuant to the determination of the Court, as set forth in its Memorandum Findings of Fact and Opinion, entered Sept. 23, 1946, it is

Ordered and Decided: That there is no deficiency in income-tax for the calendar year 1941.”

That the findings and decision in docket 6263 was a final adjudication in favor of said Jennie Wolf and against the Commissioner of Internal Revenue. The interest of Sam Schnitzer, Rose Schnitzer, Harry J. Wolf and Jennie Wolf in said Alaska Junk Company were exactly the same in the calendar years 1942 and 1943 as in the year 1941, and the fact that each of the said persons has said interests in said partnership during said years has become *res judicata* and the Respondent ought to be and is estopped to deny the same.

/s/ ROBT. T. JACOB,  
Counsel for Petitioner.

Granted June 10, 1948.

/s/ LUTHER A. JOHNSON,  
Judge.

Filed June 10, 1948, T.C.U.S.



[Title of Tax Court and Cause.]

ANSWER TO AMENDMENT TO PETITION

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and for answer to the amendment to petition filed by the above-named petitioner admits and denies as follows:

V-(a.1). Admits the allegations contained in subparagraph (a.1) of paragraph V of the petition except those contained in the last two sentences thereof which are denied.

/s/ CHARLES OLIPHANT,  
Chief Counsel, Bureau of  
Internal Revenue.

Of Counsel:

B. H. NEBLETT,  
Division Counsel;

JOHN H. PIGG,  
LEONARD A. MARCUSSEN,  
Special Attorneys,  
Bureau of Internal Revenue.

Served July 29, 1948.

Received and filed July 28, 1948, T.C.U.S.

The Tax Court of the United States  
Washington

Docket No. 14372

ESTATE OF JENNIE WOLF, Deceased, by  
Monte L. Wolf, Administrator de bonis non  
with the will annexed of said Estate,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

DECISION

Pursuant to Opinion of the Tax Court promulgated July 14, 1949, the respondent filed a computation on October 6, 1949, and the petitioner, on November 7, 1949, filed an acquiescence in the computation as filed by the respondent. Now, therefore, it is

Ordered and Decided: That there is a deficiency in income and victory tax due from this petitioner for the calendar year 1943 in the amount of \$42,273.99.

/s/ LUTHER A. JOHNSON,  
Judge.

Entered Nov. 9, 1949.

Served Nov. 10, 1949.

In the United States Court of Appeals  
For the Ninth Circuit

T. C. Docket No. 14372

ESTATE OF JENNIE WOLF, Deceased, by  
MONTE L. WOLF, Administrator de bonis  
non with the Will annexed, of said Estate,  
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

### PETITION FOR REVIEW

Comes now the petitioner, by his attorneys of record, and respectfully shows this Honorable Court:

#### I.

The petitioner is the duly appointed, qualified and acting administrator de bonis non with the will annexed of the estate of Jennie Wolf, deceased, and he is the former executor of said estate. He resides at 3410 S.E. Woodstock Boulevard, Portland, Oregon, and has his place of business at 900 S.W. First Avenue, Portland, Oregon. The return for the period here involved was filed by Jennie Wolf with the Collector of Internal Revenue for the District of Oregon.

#### II.

The respondent is the duly appointed, qualified and acting Commissioner of Internal Revenue of

the United States and is hereinafter referred to as the "Commissioner."

### III.

The taxes in controversy are income and victory taxes for the calendar year 1943.

### IV.

#### Nature of Controversy

For many years prior to and during the taxable year before the court Sam Schnitzer, Harry J. Wolf, Rose Schnitzer and Jennie Wolf were doing business as copartners under the name and style of Alaska Junk Company. During the years 1942 and 1943 Alaska Junk Company was engaged in the business of buying, selling and generally dealing in junk, pipe, tools, machinery, hardware, scrap and other metals, and as a part of its regular business, made loans and advances to customers and affiliated enterprises, always treating these loans and advances as "accounts receivable" on its books of account.

Morris Schnitzer, a son of Sam Schnitzer, was engaged in a similar business and in 1941 organized the Oregon Electric Steel Rolling Mills (hereinafter referred to as "Oregon Steel") an Oregon corporation, to manufacture steel products. The company's authorized capital was 2,500 shares having a par value of \$100.00 each, a total capital of \$250,000.00. Upon final distribution of this stock the

partners of Alaska Junk Company received 1,249 shares and Morris Schnitzer 625 shares.

From October, 1941, to November, 1943, Alaska Junk Company advanced to Oregon Steel, cash \$327,870.23, paid bills of \$166,340.16 and furnished goods at market prices to the amount of \$347,341.62, making a total of \$841,552.01. All of these items were charged on Alaska Junk Company's books as "accounts receivable" from Oregon Steel. On the books of Oregon Steel these items were entered as "accounts payable." Alaska Junk Company received payments of cash \$114,519.88, received stock of a par value \$124,900.00 and debenture notes of a face value of \$174,000.00 making total receipts of \$413,419.88, which items were credited to said accounts receivable.

Morris Schnitzer and Alaska Junk Company orally agreed that Morris Schnitzer would bear  $\frac{1}{3}$  of the total loss, if any, that might be sustained by Morris Schnitzer and Alaska Junk Company from advances to Oregon Steel over and above the advances credited to stock subscriptions. Alaska Junk Company in turn agreed to bear  $\frac{2}{3}$  of any such loss.

Alaska Junk Company was induced to make the advances, sell goods on credit and pay the bills of Oregon Steel upon a promise of early repayment, based upon engineering estimates of minimum earnings of \$50,000.00 per month and a production schedule to begin early in 1943.

In June, 1943, Morris Schnitzer was inducted



into military service and Oregon Steel was unable to obtain competent management. As a result of this and other difficulties the operations were unsuccessful, and in November, 1944, ceased. It was then decided by the stockholders to withdraw from the enterprise, and Oregon Steel stock was then sold. Prior to the sale Oregon Steel issued Alaska Junk Company its promissory note for \$427,843.87, the balance of its account receivable, and issued its note of \$26,829.28 to Schnitzer Steel Products Company (Morris Schnitzer). In exchange for these two notes Alaska Junk Company and Morris Schnitzer received a third mortgage note for \$151,000.00. This compromise resulted in a total loss of \$303,625.90 and by reason of the agreement between Morris Schnitzer and Alaska Junk Company, Alaska Junk Company sustained a loss of \$202,350.60, which was charged off as a bad debt.

On the partnership's return for 1943 a deduction of the \$202,350.60 was claimed as a bad debt. It is this amount which the Commissioner has disallowed as a deduction. The Commissioner's contention was upheld by the Tax Court of the United States and petitioner submits that in making its determination the Tax Court was in error.

## V.

The petitioner designates the following points on which he intends to rely on appeal to the United States Court of Appeals for the Ninth Circuit from the decision heretofore entered by the Tax Court of the United States:

1. The Tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the partnership in which petitioner's transferror was a partner was not deductible as a bad debt in computing net income subject to taxation.

2. The Tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the partnership in which petitioner's transferror was a partner was not a bad debt.

3. The Tax Court erred in holding that all of the advances, including said sum of \$202,350.60, of the partnership in which petitioner's transferror was a partner were contributions to capital.

4. The Tax Court erred in not finding and holding that all of said sum of \$202,350.60 was a loan made by the partnership in which petitioner's transferror was a partner.

5. The decision entered by the Tax Court herein is not supported by the evidence, is contrary to the evidence and is in disregard of it.

6. The Tax Court erred in determining that there was a deficiency in income and victory taxes for the calendar year 1943 due from the above named petitioner.

Wherefore, the petitioner petitions that the decision of the Tax Court of the United States be reviewed by the United States Court of Appeals for the Ninth Circuit; that a copy of the record on review be prepared in accordance with law and with the rules of said Court and transmitted to the Clerk

of said Court for filing and that appropriate action be taken by said Court to review and correct the decision of the Tax Court which petitioner submits is erroneous.

/s/ ROBERT T. JACOB,  
/s/ RANDALL S. JONES,  
Attorneys for Petitioner.

Received and filed January 4, 1950, T.C.U.S.

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In the United States Court of Appeals  
for the Ninth Circuit

T. C. Docket No. 14372

ESTATE OF JENNIE WOLF, Deceased, by  
MONTE L. WOLF, Administrator de bonis  
non With the Will Annexed, of Said Estate,  
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

NOTICE OF FILING OF PETITION FOR  
REVIEW

To: Charles Oliphant, Chief Counsel for the Bureau of Internal Revenue.

You will please take notice that on the 4th day of January, 1950, the petitioner above named filed with the Clerk of the Tax Court of the United States at Washington, D. C., a Petition for Review by the United States Court of Appeals for the Ninth Cir-

cuit of the decision of the Tax Court of the United States heretofore entered in the above-entitled proceeding.

A copy of said Petition for Review as filed is attached hereto and served upon you.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES.

Receipt of copy acknowledged.

Received and filed January 9, 1950.

The Tax Court of the United States  
Washington

[Title of Cause.]

### CERTIFICATE

I, Victor S. Mersch, Clerk of The Tax Court of the United States do hereby certify that the foregoing documents, 1 to 12, inclusive, constitute and are all of the original papers and proceedings before the Tax Court of the United States as set forth in the "Designation of Record" except the original exhibits 1-27, incl., 28, 30, 31, 33-36, incl., 65, 66, 72-79, incl.; 65, 66, 72-79, incl.; A-Z, AA-HH, incl., on file in my office as the original record in the proceeding and in which the petitioner in The Tax Court proceeding has initiated an appeal as above numbered and entitled, together with a true copy of the docket entries in said Tax Court proceeding, as the same appear in the official docket book in my office.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia, this 23rd day of January, 1950.

[Seal]      /s/ VICTOR S. MERSCH,  
Clerk.

[Endorsed]: No. 12476, United States Court of Appeals for the Ninth Circuit. Estate of Jennie Wolf, deceased, by Monte L. Wolf, Administrator de bonis non with the will annexed of said Estate, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Petition to Review a Decision of The Tax Court of the United States.

Filed February 7, 1950.

              /s/ PAUL P. O'BRIEN,  
Clerk of the United States Court of Appeals for the  
Ninth Circuit.

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In the United States Court of Appeals  
for the Ninth Circuit

T. C. Docket No. 14208

SAM SCHNITZER,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

T. C. Docket No. 14209

ESTATE OF HARRY J. WOLF, Deceased, by  
MONTE L. WOLF, Administrator de bonis  
non with the will annexed of said Estate,  
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

T. C. Docket No. 14278

MONTE L. WOLF,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

T. C. Docket No. 14279

BLOSSOM M. GOLDSTEIN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14280

CHARLOTTE C. COHON,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

T. C. Docket No. 14372

ESTATE OF JENNIE WOLF, Deceased, by

MONTE L. WOLF, Administrator de bonis

non with the will annexed of said Estate,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

## MOTION TO CONSOLIDATE APPEALS

The above named petitioners on review and each of them, acting by and through their attorneys of record, hereby move this court to consolidate the above entitled proceedings for purposes of the printed record on appeal, the briefing, the hearing,

the argument, the decision and for all other purposes connected with the final disposition of said proceedings on review.

This motion is based on the grounds that all of the above entitled proceedings were consolidated for trial below in the Tax Court, that the Tax Court made but one set of findings of fact and rendered but one opinion in connection with all of these cases, that each of these cases involves the same facts, that each of the petitioners on review was either a partner or is now the transferee of a decedent who was a partner in a partnership known as the Alaska Junk Company, that the sole question for decision concerns the deductibility of a bad debt by said Alaska Junk Company, and that the decision on this single point is determinative of the income tax liability of each of said partners or said transferees of partners who are the petitioners herein.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,

917 Public Service Building,  
Portland 4, Oregon.

I, Randall S. Jones, being on oath first duly sworn, depose and say:

That on the 13th day of February, 1950, I served the foregoing Motion to Consolidate Appeals upon Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, by on said day depositing a duly certified copy thereof in the United

States mails with full postage and registration charges prepaid, addressed to Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, Internal Revenue Building, Washington, D. C. Said papers were deposited in the United States mails at the Federal Post Office, S. W. Sixth and Main Streets, Portland 4, Oregon.

/s/ RANDALL S. JONES.

Subscribed and sworn to before me this 13th day of February, 1950.

[Seal] /s/ JACQUELINE MOHLAND,  
Notary Public for Oregon.

My commission expires: 9-22-52.

So Ordered:

/s/ WILLIAM DENMAN,  
Chief Judge.

/s/ HOMER BONE,

/s/ WM. E. ORR,

U. S. Circuit Judge.

[Endorsed]: Filed Feb. 15, 1950.

[Title of Court of Appeals and Causes.]

STATEMENT OF POINTS ON WHICH  
PETITIONERS INTEND TO RELY

The petitioners on review hereby enumerate the points on which they intend to rely on appeal and which are as follows:

1. The Tax Court erred in holding that the sum of \$202,350.60 charged off as a bad debt by the partnership in which petitioners were partners was not a bad debt and not deductible in computing the net income of said partnership and petitioners' net income subject to taxation for the taxable year 1943.

2. The Tax Court erred in holding that the total, or any amount in excess of \$125,000.00, representing bills paid for, cash advanced to, and goods sold to Oregon Electric Steel Rolling Mills by the partnership in which petitioners or their transferrors were partners, constituted a contribution to the capital of said Oregon Electric Steel Rolling Mills.

3. The Tax Court erred in not finding and holding that all and every part of said sum of \$202,350.60 was a debt owed to the partnership in which petitioners were partners.

4. The decision entered by the Tax Court herein is contrary to the law, the Tax Court's findings of fact, and the evidence; and is not supported by said findings of fact or the evidence and is in disregard of both said findings of fact and the evidence.



5. The Tax Court erred in failing to include in its findings material facts clearly established by the evidence which further show that the bills paid, cash advanced and goods sold to Oregon Electric Steel Rolling Mills constituted an indebtedness owed to the partnership.

6. The Tax Court erred in admitting respondent's exhibits O, P, Q, U, V, AA, FF, GG and HH over objections of petitioner for the reasons set forth respectively on pages 120, 121, 122, 129, 134, 137, 495, 589-591, 621 and 636, 639 and 640 of the *Report's* Transcript of the Proceedings before said court.

7. The Tax Court erred in receiving oral testimony adduced by respondent over objections of the petitioners as set forth in those portions from the Reporter's Transcript of the Proceedings before said court which the petitioners have designated for inclusion in the Printed Record.

8. The Tax Court erred in sustaining objections of the respondent to questions asked by petitioners and to oral testimony offered by petitioners, which questions, objections and rulings thereon are set forth in those portions from the Reporter's Transcript of the Proceedings before said court which

the petitioners have designated for inclusion in the Printed Record.

/s/ ROBERT T. JACOB,

/s/ RANDALL S. JONES,  
917 Public Service Bldg.,  
Portland 4, Oregon.

I, Randall S. Jones, being on oath first duly sworn, depose and say:

That on the 13th day of February, 1950, I served the Statement of Points on which Petitioners Intend to Rely upon Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, by on said day depositing a duly certified copy thereof in the United States mails with full postage and registration charges prepaid, addressed to Charles Oliphant, Chief Counsel, Bureau of Internal Revenue of the United States, Internal Revenue Building, Washington, D. C. Said papers were deposited in the United States mails at the Federal Post Office, S. W. Sixth and Main Streets, Portland 4, Oregon.

/s/ RANDALL S. JONES.

Subscribed and sworn to before me this 13th day of February, 1950.

[Seal] /s/ JACQUELINE MOHLAND,  
Notary Public for Oregon.

My commission expires: 9-22-52.

[Endorsed]: Filed Feb. 15, 1950.



**In the United States**  
**COURT OF APPEALS**  
**for the Ninth Circuit**

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SAM SCHNITZER,

ESTATE OF HARRY J. WOLF, Deceased, by  
Monte L. Wolf, Administrator, de bonis non  
with the will annexed of said estate,

MONTE L. WOLF,

BLOSSOM M. GOLDSTEIN,

CHARLOTTE C. COHON,

ESTATE OF JENNIE WOLF, Deceased, by Monte  
L. Wolf, Administrator de bonis non with the  
will annexed of said estate,

*Petitioners,*

vs.

COMMISSIONER OF INTERNAL REVENUE,  
*Respondent.*

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**BRIEF FOR THE APPELLANT**

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On Appeal from the Tax Court of the United States.

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ROBT. T. JACOB and  
JACOB & BROWN,

*Attorneys for Petitioners.*

GARTHE BROWN,  
*Of Counsel.*

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FILED STEVENS-NEWELL LAW P.B. CO., PORTLAND

4-50

APR 20 1950

PAUL P. O'BRIEN





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**In the United States**  
**COURT OF APPEALS**  
**for the Ninth Circuit**

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SAM SCHNITZER,

ESTATE OF HARRY J. WOLF, Deceased, by  
Monte L. Wolf, Administrator, de bonis non  
with the will annexed of said estate,

MONTE L. WOLF,

BLOSSOM M. GOLDSTEIN,

CHARLOTTE C. COHON,

ESTATE OF JENNIE WOLF, Deceased, by Monte  
L. Wolf, Administrator de bonis non with the  
will annexed of said estate,

*Petitioners,*

vs.

COMMISSIONER OF INTERNAL REVENUE,

*Respondent.*

---

**BRIEF FOR THE APPELLANT**

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On Appeal from the Tax Court of the United States.

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**CONSOLIDATION OF APPEALS**

On motion of petitioners, on February 15, 1950 this  
Court ordered that the above entitled proceedings be  
consolidated for purposes of the printed record, brief,



hearing, argument, decision and all other purposes connected with the final disposition of said proceedings (R. 547-549).

## JURISDICTION

This appeal is from a decision of the Tax Court of the United States entered November 9, 1949 (R. 71).

On March 3, 1947 the Commissioner of Internal Revenue mailed petitioners, Sam Schnitzer, Harry J. Wolf and the Estate of Jennie Wolf, Notices of Deficiency in income and victory taxes for the taxable year 1943 (R. 16) and on March 4, 1948 said Commissioner mailed notices to Monte L. Wolf, Blossom M. Goldstein and Charlotte C. Cohon covering proposed deficiencies in income and victory taxes for the taxable year 1943 as transferees of the estate of Jennie Wolf, who died on April 8th, 1945 and Monte L. Wolf is administrator de bonis non of her estate. Harry J. Wolf died February 6, 1948, and Monte L. Wolf is executor of his estate. Petitioners appealed to the Tax Court from these proposed deficiencies within the time provided by Section 272 of the Internal Revenue Code (R. 2 et seq.). The Tax Court's jurisdiction is set forth in Sections 1101 and 272 of the Internal Revenue Code.

As set out in the petitions for review, petitioners are residents of Portland, Oregon, and filed their income and victory tax returns with the Collector of Internal Revenue for the District of Oregon, whose office is located within the ninth judicial district, wherein petitioners also reside. This court has jurisdiction to review the

Tax Court's decision under the provisions of Sections 1141 and 1142 of the Internal Revenue Code (26 U.S.C.A., Sections 1141 and 1142) and Title 28 U.S.C.A., Section 2106.

## STATEMENT OF THE CASE

During the years 1942-1943 Sam Schnitzer and Harry J. Wolf were active in the operation of Alaska Junk, a partnership, engaged in the business of dealing generally in machinery, junk, scrap and other metal products in Portland, Oregon. The partnership books were kept on the accrual basis (R. 34).

H. J. and Jennie Wolf were married in 1906, and Mr. Wolf learned the junk business from his father-in-law, and as Mrs. Wolf was also familiar with the junk business they decided to operate independently. She had a dower of \$1,000.00 and this was used to buy a horse and wagon (R. 34). About the same time Sam Schnitzer began to deal in scrap metal, and in 1911 Wolf and Schnitzer entered the junk business as partners and operated as Alaska Junk Co. (R. 35).

As Alaska Junk expanded its activities and grew in financial strength it made loans or advances to customers in the expectation of maintaining or increasing its trade. Most of the advances were repaid in cash or scrap, but some were not (R. 38).

Alaska Junk also made "very large" advances to enterprises in which petitioners' families were interested. Some of these advances were made AS LOANS and

some for CAPITAL STOCK. Alaska Junk kept open accounts with all of the businesses to which said advances were made, charging them with cash and merchandise furnished and crediting them with cash and goods received (R. 39-40).

On June 4, 1941 Morris Schnitzer, son of Sam Schnitzer, organized the Oregon Electric Steel Rolling Mills with authorized capital of \$250,000.00 represented by 2,500 shares. On the same date Morris Schnitzer and his attorney, Louis Schnitzer, subscribed for 1,251 shares (control) and Sam Schnitzer and Harry J. Wolf each subscribed for  $312\frac{1}{2}$  shares. February 10, 1942, 1,251 shares were issued to Morris Schnitzer and  $312\frac{1}{2}$  each to Sam Schnitzer and Harry J. Wolf (R. 40-41). Oregon Steel never issued more capital than \$187,800.00 (R. 48). Oregon Steel was organized to erect and operate a mill to roll steel products. Petitioners expected it to provide a local market for their scrap, and engineers estimated it would eventually earn \$50,000.00 or more per month. Morris Schnitzer, educated in engineering and business administration and with wide experience in related operations, originated the idea and arranged for organization and financing of Oregon Steel (R. 41).

Alaska Junk made large advances, supplied merchandise and paid bills for Oregon Steel, and charged same to an open account with that company. All such charges were credited to Alaska Junk by Oregon Steel (R. 42).

Morris Schnitzer made numerous attempts to procure outside capital (R. 43). RFC finally approved a loan of \$700,000.00 (R. 44). Payment of this loan was

guaranteed by petitioners, who also agreed to supply "additional working capital" and not to require payment of their advances during pendency of the loan except in common stock or debenture notes (R. 45). RFC did repay \$114,519.88 of these advances (R. 46).

Alaska Junk obtained an agreement from Morris Schnitzer to assume one-third of any loss which might be jointly sustained by reason of advances, and March 11, 1943, Alaska Junk took over one-half of his stock (R. 47), Morris having received his second notice of induction into the armed forces February, 1943 (R. 92). Oregon Steel was unable to obtain a competent manager. It experienced great difficulty in getting into operation and closed down November, 1943. The stockholders sold their stock for 1¢ per share. Before doing so Oregon Steel gave Alaska Junk its note for \$427,843.87, and Morris Schnitzer a note for \$26,829.28 (R. 49-50).

Purchasers elected new officers and directors and with consent of RFC Oregon Steel gave its note for \$249,000.00 secured by second mortgage and its note for \$151,000.00 secured by third mortgage. By accepting notes for \$151,000.00 for previously issued notes the five stockholders of Oregon Steel lost \$303,625.90 due for advances on open account, which account at that time showed balance of \$454,625.90. Based upon compromise of the debts, Alaska Junk lost \$202,350.60, and this amount was charged off as a bad debt (R. 51-52).

This loss is the subject matter of this appeal. The respondent disallowed the deduction and the Tax Court sustained his position.



## SPECIFICATION OF ERRORS

### I.

The Tax Court erred in holding that the bad debt of \$202,350.60 charged off by the partnership in which petitioners were partners was not a bad debt and not deductible in computing petitioners' taxable net income for the year 1943.

### II.

The Tax Court erred in holding that the total, or any amount in excess of \$125,000.00, representing bills paid for, cash advanced to, and goods sold to Oregon Electric Steel Rolling Mills by Alaska Junk Co. constituted a contribution to the capital of said Oregon Electric Steel Rolling Mills.

### III.

The Tax Court erred in not finding and holding that the entire sum of \$202,350.60 was a debt owed to Alaska Junk Co.

### IV.

The Tax Court's decision herein is contrary to law, the findings of fact and the evidence; it is not supported by said findings of fact or the evidence, but is in disregard of both said findings and evidence.

### V.

The Tax Court made the following finding:

"From October, 1941 Alaska Junk made numerous advances of cash to Oregon Steel; supplied it with goods of various kinds 'at cost' and paid bills for it. . . . On an office memorandum Sam Schnitzer referred to these advances as 'contributed capital'."



The Tax Court erred in finding: (a) that the goods which Alaska Junk supplied to Oregon Steel were supplied at cost, (b) that Sam Schnitzer ever wrote an office memorandum referring to the advances as "contributed capital" or using words of similar import.

## VI.

The Tax Court erred in failing to include in its findings the following material facts:

(a) Alaska Junk made advances of merchandise, services and cash to National Machinery Company, a subsidiary corporation. Subsequently the latter concern was liquidated, and the unpaid account of \$30,-437.17 was charged off as a bad debt by Alaska Junk and deducted on its tax return and allowed by the Commissioner (R. 198-199, 292-293, 360-362).

(b) Hesse-Ersted Company, which ran a machine shop, was in serious financial straits in 1941. Alaska Junk assisted it financially by loaning it \$65,000.00, to enable it to complete a large contract. As a result Alaska Junk secured Hesse-Ersted as a substantial customer, whereas prior to that time dealings with it had been only casual (R. 188-189, 236-237, 321).

## VII.

The Tax Court erred in determining that there was a deficiency in income and victory taxes for the calendar year 1943 due from petitioners herein.

## STATUTES INVOLVED

Set forth in the appendix, *infra*.

## SUMMARY OF ARGUMENT

### I.

#### Introductory

##### 1. THE ISSUE.

There is but a single, simple issue: Were advances made by the stockholders through their business partnership to Oregon Steel, in accordance with a long established practice of making such advances for increasing the partnership's business, capital contributions or debts?

##### 2. PETITIONERS' BUSINESS INCLUDES MAKING ADVANCES AS LOANS.

Petitioners' partnership, Alaska Junk, was organized in 1911, and over its thirty years of operation it had made a practice of making advances to business enterprises for increasing its business.

##### 3. THE LOSS DEDUCTION AROSE FROM SETTLEMENT OF THE DEBT.

After Morris Schnitzer (the promoter and owner of controlling stock of Oregon Steel) was called into military service, Oregon Steel fell apart and the stockholders decided to sell their stock. The corporation, by its new officers, compromised the debt by giving a note secured by a third mortgage on Oregon Steel's real and personal property on the basis of its indebtedness to the former stockholders and not on the basis of stock ownership.

## II.

### The Trier's Findings of Fact

#### 1. THE PRIMARY FACTS FOUND ARE CORRECT IN THE MAIN.

The following findings are excepted to:

(a) That on an office memorandum Sam Schnitzer referred to the advances as "contributed capital";

(b) That the goods which Alaska Junk supplied to Oregon Steel were supplied "at cost";

(c) That the court failed to find that included amongst the concerns to which Alaska Junk made advances were National Machinery Company, a subsidiary corporation, and Hesse-Ersted Company, a large user of petitioners' merchandise.

#### 2. PRIMARY FACTS FOUND REQUIRE ULTIMATE FINDING THAT THE CONTROVERTED ADVANCES WERE DEBTS.

The primary facts found by the court expressly include all of the essential elements of an indebtedness and the loss resulting therefrom; the advances were made and merchandise sold; the funds and merchandise were accepted; the books of the vendor and vendee recorded the transactions as accounts receivable and accounts payable respectively; \$114,519.88 of the advances were repaid by RFC; all entries conform to the established method of creating debtor-creditor relationship; and the debt was recognized and settled by compromise payment.

### III.

#### **Trial Court's Erroneous Findings and Conclusions**

##### 1. ERRONEOUS INFERENCES DRAWN FROM PRIMARY FACTS.

An analysis of the various evidentiary facts upon which the court apparently relied as a basis for its adverse inferences clearly shows that said inferences are based upon a misconstruction of the evidence and are in direct contradiction to positive, primary facts competently found.

##### 2. THE TRIER'S ERRORS OF LAW.

Also, an analysis of the factors considered and the rules of law applied by the trier demonstrates an equally gross misconception of the legal principles governing the determination of the issue.

### IV.

#### **Review of the Entire Record to Determine Error**

It is submitted that even though upon consideration of the primary facts found by the trial court, this court concludes these facts support the ultimate findings, nevertheless under the present FRCP and the decisions relating thereto this court must review the entire record to determine whether a mistake has been committed; the only limitation upon this review is that a conflict in the oral testimony of witnesses will not be resolved.

## ARGUMENT

### I.

#### Introductory

##### 1. THE ISSUE.

A single issue is presented. Were open account advances debts or capital contributions?

Within the last year this court has twice passed upon the issue involved in the instant case. In *Maloney v. Spencer*, 172 F. 2d 638 (C.C.A. 9th, 1949), Chief Judge Denman wrote a comprehensive opinion on the question of advances by a stockholder to his wholly owned corporations. In *Wilshire & Western Sandwiches, Inc. v. Commissioner*, 175 F. 2d 718 (C.C.A. 9th, 1949), Judge Orr also fully discussed the law applicable to the issue.

##### 2. PETITIONERS' BUSINESS INCLUDES MAKING ADVANCES AS LOANS.

In order for the issue involved to be rationally and fairly resolved, it must be considered in the business setting surrounding the controverted transactions.

Through their partnership, Alaska Junk, petitioners made advances to Oregon Steel in accordance with a long established business practice of making such advances "in the expectation of increasing or expanding their business". Were these advances INTENDED TO ENLARGE THE CAPITAL of Oregon Steel, or were they INTENDED TO CREATE A DEBT?



There is no intimation that the controversial transactions involve sham, artifice or the "statutory literalness" condemned in *Gregory v. Helvering*, 293 U.S. 465 (1935). Nor is tax avoidance so much as hinted at. Also, the facts present a much stronger case for petitioners than the single, isolated, stock-note transactions involved in tax avoidance cases, such as *Janeway v. Commissioner*, 147 F. 2d 602 (C.C.A. 2d, 1945); 1432 *Broadway Corporation v. Commissioner*, 160 F. 2d 885 (C.C.A. 2d, 1947); *Mullin Building Corporation*, 9 T.C. 350 (1947). The challenged advances were made by a partnership engaged in business, as distinguished from an individual not engaged in a trade or business, and such advances were made in conformity with a long established business practice; they were only incidentally connected with a stock subscription; and in a compromise settlement of the debt the petitioners received 33.2141% of the account. The entire course of petitioners' conduct and their actions throughout point to a single purpose and intention, and there is nothing therein to cast doubt on the existence of the debtor-creditor relationship.

Petitioners had a large business and they stood high in the community. E. B. McNaughton, Chairman of Board of the First National Bank of Portland, called by respondent, in referring to Sam Schnitzer and Harry J. Wolf, testified (R. 441):

"These men were phenomenal successes as salvage merchandise dealers, starting at almost pushcart level, and they had worked themselves up to be one of the most successful clients or customers the bank had; . . ."

A. W. Groth, Vice President of the same bank, also respondent's witness, testified (R. 489):

" . . . In the case of responsible people, such as the Schnitzers and Wolfs with whom we have had business dealings over a period of years, and who have always worked in close cooperation with us and in entire honesty with the bank, we would take their word for it, whatever they would say."

(R. 496):

"We had confidence in the Schnitzer family and the Wolf family, based on many years of successful banking experience, and we took their word."

We find adequate recitals in the court's findings of the growth and development of petitioners' business.

Petitioners, Harry J. Wolf and Sam Schnitzer, began in the junk business as early as 1906. Wolf used his wife's dowry to buy a horse and wagon, which in 1911 he contributed to a partnership called Alaska Junk Co., and toward which Schnitzer paid about \$1,000.00. This partnership continued in the business of buying, selling and generally dealing in junk, pipe, tools, machinery, hardware, scrap and other metal products, and kept its books on the accrual basis.

As Alaska Junk expanded its activities and grew in financial strength it made loans or advances to customers and to enterprises in which petitioners were interested, in the expectation of maintaining or increasing its trade. Stock was subscribed and paid for in some of these enterprises in identically the same manner as the instant transaction. The partnership kept open accounts with all the persons to whom advances were made and

merchandise sold, charging to such accounts all cash and merchandise and crediting them with payments.

On June 4, 1941 Morris organized Oregon Steel with authorized capital \$250,000.00, represented by 2,500 shares. On that date stock was subscribed for and on February 10, 1942 1,251 shares (control) were issued to Morris Schnitzer and 312 $\frac{1}{2}$  each to Sam Schnitzer and Harry J. Wolf.

Oregon Steel was to erect and operate a rolling mill for the manufacture of steel products, from scrap metal, and on the basis of engineers' estimates expected earnings of \$50,000.00 or more a month. Morris Schnitzer originated and headed the project. He was experienced in merchandising iron, steel, tools and machinery and salvage enterprises throughout the country, and was educated in engineering and business administration.

From October, 1941 (more than four months after the stock subscription) Alaska Junk made numerous advances of cash to Oregon Steel, supplied it with goods of various kinds and paid bills for it and charged these items to Oregon Steel on open account. All charges were reflected by corresponding credits on Oregon Steel's books.

These facts, competently established, create a business background of honesty, integrity and successful dealings which must be given full significance in the determination of the issue involved. The controverted transaction is simply one in a long series of identical transactions entered into by the petitioners through their partnership, Alaska Junk (using the literal language of

the court) "in the expectation of maintaining or increasing its trade," and it is strikingly unlike the situations in which a single stockholder or a family group suddenly realizes that by reorganizing their corporation and substituting notes or bonds for capital stock they may obtain interest in lieu of dividends and thereby provide the corporation with a tax deduction. Nor is this a case where tax considerations entered into the transaction in any particular, but the transaction follows a pattern of long standing.

By 1941 Alaska Junk had become a large dealer in scrap metal and was obtaining an inadequate price for it. Morris Schnitzer, an ambitious young man with business education and experience, proposed to establish a rolling mill operation as an outlet for this scrap. He consulted engineers and obtained data which indicated monthly profits of \$50,000.00 or more; he interested his father and his father interested his partner, Wolf, who proved to be a reluctant participant, but step by step he was led to agree to permit the partnership to subscribe for a maximum of \$125,000.00 of Oregon Steel stock. Obviously without any instructions from the petitioners to record the transactions with a view to laying the foundation for a "tax loss," the bookkeepers of Alaska Junk and of Oregon Steel simultaneously recorded the transactions identically as all previous transactions of the same kind had been recorded. Undoubtedly the trial court completely lost sight of these significant facts which he so clearly recorded in arriving at his conclusion that the advances were paid in as risk capital and not as loans.



### 3. THE LOSS DEDUCTION AROSE FROM THE SETTLEMENT OF A DEBT.

When Hall and Mears purchased Oregon Steel's stock and elected a new board of directors, the advances were still a liability (an account payable) of Oregon Steel, and the debt represented by this account payable was settled on behalf of the new owners of Oregon Steel by the execution of a SECURED note for \$151,000.00 covered by a third mortgage on the company's real and personal property. The account is at this point recognized as a debt. No change took place in it from its inception, yet the court treated it as a capital contribution. Was a "capital contribution" then converted to a debt? Did the "leopard change its spots"?

Petitioners' Exhibit 22, Minutes of Special Meeting of Directors of Oregon Steel of Nov. 26, 1943, contains the following:

"The said S. Schnitzer then stated that the Oregon Electric Steel Rolling Mills was then indebted to the Alaska Junk Company in the sum of \$427,843.87, as evidenced by a note dated November 26, 1943, and that the corporation was then further indebted to Schnitzer Steel Products, of which Morris Schnitzer is the sole owner, in the sum of \$26,829.28, as evidenced by promissory note dated November 26, 1943.

"It was agreed that the holders of said notes would compromise said indebtedness for the sum of \$151,000.00, to be evidenced by a promissory note secured by a third mortgage on the corporation's real property and most of its personal property. A proposed form of note and third mortgage was then submitted. An exhibit describing the personal property to be specifically mortgaged was attached to the form of mortgage.



"On motion duly made and seconded and adopted by unanimous vote, it was

"RESOLVED that the President and Secretary of the corporation be and are hereby authorized and directed to execute said note and third mortgage in exchange for the surrender of the above described promissory note.

"Thereupon said note and mortgage were executed by the President and Secretary of the corporation and were duly offered in compromise and surrender of said promissory notes. The offer was accepted and the said promissory notes were then and there surrendered in consideration of the delivery of said note and third mortgage."

It is particularly significant to this issue that the new owners of the stock recognized the obligation of Oregon Steel to the Alaska Junk as an indebtedness and accepted an offer to compromise said indebtedness for \$151,000.00 and agreed to issue a note for this amount (secured by a mortgage on the corporation's real and personal property) in full satisfaction of the indebtedness. They had paid only 1¢ per share of \$100.00 for the stock of Oregon Steel. (Loss from the sale of the stock is not involved in this case.)

In *Maloney v. Spencer*, 172 F. 2d 638 (C.C.A. 9th, 1949), this court in citing with approval *Van Clief v. Helvering*, 135 F. 2d 254, 256, copied the court's quotation from *Edward Katzinger Co. v. Commissioner*, 44 B.T.A. 533, 536, as follows:

" . . . Here the parties intended the advances as loans. This is shown not only by the testimony of the officers, *but by the entries on the books of the two companies and the consistent actions of the parties in regard to the advances, including their*

*actions incident to the liquidation'.*" (Italics supplied)

In copying this quotation this court italicized the portion of the sentence relating to the entries on the books, the consistent actions of the parties in regard to the advances and their actions incident to the *liquidation of the corporation*. This emphasizes the petitioners' position, as all the factors considered in that case are present here and are strengthened by the clear, uncontradicted testimony of several witnesses as to the intention of the petitioners.

Refer further to paragraph 31 of stipulation (R. 535), which reads in part:

"On November 26, 1943, Oregon Steel executed and delivered to Alaska Junk a promissory note in the amount of \$427,843.87 as evidence of the advances made to it by Alaska Junk as of that day, shown by the books of Oregon Steel. Exhibit 20 is a photostatic copy of said note. . . ."

As stated in the stipulation, this note was given "as evidence of the advances made to it by Alaska Junk." Thus the respondent admits that the note which was compromised and settled evidenced the advances thereby recognizing the debtor-creditor relationship.

The note, Exhibit 20, bears this endorsement on its face:

"Compromised and cancelled in consideration of delivery of third mortgage."

## II.

### The Trier's Findings of Fact

#### 1. THE PRIMARY FACTS FOUND ARE CORRECT IN THE MAIN.

Notwithstanding the correctness of many primary facts found, the court seriously erred in the following particulars:

(a) The court found (R. 43):

"On an office memorandum Sam Schnitzer referred to those advances as 'contributed capital'."

There is no evidence in the record upon which to base this finding, but it is evident the court's conclusions were influenced by it. It refused to accept the testimony of petitioners' witnesses on this point on the ground that the statements and conduct of petitioners did not support their testimony. Obviously this finding aided in directing the court's thinking to the prejudice of petitioners.

(b) The court also found (R. 42):

"From October, 1941 Alaska Junk made numerous advances of cash to Oregon Steel; supplied it with goods of various kinds at cost. . . ."

This finding is clearly contrary to the record.

Morris Schnitzer, the promoter and manager of Oregon Steel, testified (R. 95):

"Q. At what prices, when Oregon Steel bought from Alaska—— what prices did you pay to Alaska for merchandise out of their stock?

A. We paid the standard prevailing price.

Q. . . . I want to call your attention to the things that were purchased for the construction of the mill before you went into the service; do you know on what basis or on what price that merchandise was purchased?

A. We paid the standard prices for what was purchased, which standard prices were gauged by the Moore Book, which was the book that the Portland Jobbers Association paid, or what they went by. That was for scrap. For new steel that was fabricated, we paid the jobbers' price; for electric motors and so forth, the same."

(R. 370) After explaining his duties with Alaska Junk and the pricing of merchandise, Monte L. Wolf testified (R. 371):

"Q. At what price was the merchandise sold to Oregon Steel?

A. At the regular prevailing market prices. Piping is based upon Moore's Pricing Manual."

Insofar as the sale of merchandise to Oregon Steel is concerned, Alaska Junk was in identically the same position as though it were dealing with outside parties. It was dealing "at arm's length" as to merchandise furnished, which amounted to \$347,341.62. To that extent it found an outlet for its merchandise, realized its normal profit and paid to the government its regular taxes thereon. If the stock subscription were not involved, there could be no question raised about the validity of petitioners' claim for the deduction of the challenged loss. We say that the other circumstances complained of by the court do not affect petitioners' rights and have not, in any wise, changed their status as bona fide credi-



tors under the obligation created by supplying the merchandise, cash and credit.

(c) The court failed to make any finding with respect to the advances made to National Machinery Company, a subsidiary corporation, and Hesse-Ersted Company, a large outlet for petitioners' merchandise. This omitted finding is another indication of the court's lack of full knowledge of the evidence in the record. Manuel Schnitzer testified (R. 198):

"Q. Did the Alaska Junk Company have any business relation with the National Machinery Company?

A. Yes.

Q. What?

A. We sold them a tremendous amount of merchandise.

Q. Did you ever supply them any cash?

A. Yes."

M. R. Schnitzer testified (R. 292):

"The Court: How many sheets are there?

The Witness: Forty-nine pages. . . . Total pages; that is the original records of the Alaska Junk Company accounts receivable with the National Machinery Company of Eugene. . . (R. 293) It is the record of the merchandise and cash advances to the National Machinery Company of Eugene, which was a subsidiary corporation of the Alaska Junk Company, for the period of January 1, 1928 until December 31, 1933, when it was written off and closed."

(R. 360):

"Q. I am handing you National Machinery Company account, and I want you to state whether there was a bad debt there?

A. Yes, we wrote off \$30,000 odd in 1933."



Following the above testimony the witness testified that the bad debt loss on account of National Machinery Company of \$30,437.17 was deducted on the 1933 Federal tax return and was allowed in the Revenue Agent's report on behalf of the Commissioner (Ex. 56). The court's failure to make a finding with respect to this deduction of a bad debt loss in connection with a subsidiary company of the Alaska Junk Company is another circumstance in the chain which influenced the court in its adverse holdings.

Regarding the Hesse-Ersted account, reference is made to the testimony of Manuel Schnitzer. After naming Hesse-Ersted Company he was asked (R. 236):

"Q. What was the nature of the advances made to them?

A. We made cash payments for them, we got a mortgage from them. . . . for \$50,000 or \$60,000."

This witness repeated his testimony at R. 189 wherein he stated that the company operated a machine shop and Alaska Junk saw an opportunity to make a profit by assisting them through buying or selling materials (R. 321). This testimony was corroborated by M. R. Schnitzer (R. 322). He further testified that Hesse-Ersted purchased machinery for their use and that that transaction was indicative of many such transactions, including Western Foundry, Vaughn Motor Works, etc.

A consideration of all of these items was necessary in order to give proper weight to the entire record, and a failure to give consideration to the record in its entirety, obviously, was seriously prejudicial to petitioners.

## 2. PRIMARY FACTS FOUND REQUIRE ULTIMATE FINDING THAT CONTROVERTED ADVANCES WERE DEBTS.

An analysis of the primary facts found by the Tax Court shows clearly that the advances were made under such circumstances as to require the conclusion they created the debtor-creditor relationship. The court's findings expressly include all the essential elements of an indebtedness and the loss therefrom, viz: the advancement of the funds, payment of bills or sale of merchandise; a meeting of the minds evidenced by acceptance and use of the funds and merchandise by the vendee; expectation of reimbursement as shown by charges on the books of the vendor; acknowledgement of the debt and agreement to pay evidenced by credits to the vendor on the books of the vendee; all entries relating to the transaction conforming to a long established practice and method of creating a debtor-creditor relationship; and settlement of the debt by compromise and partial payment.

Adopting the language of the court, it found:

“ . . . Sam Schnitzer and Harry J. Wolf were active in the operation of Alaska Junk Co. . . . a partnership engaged in . . . dealing in junk, . . . machinery, . . . scrap and other metal products . . . Its books were kept on an accrual basis, . . . (R. 33-4)

“As Alaska Junk expanded its activities and grew in financial strength, it occasionally made loans to customers in the expectation of maintaining or increasing its trade. . . . (R. 38)

“Alaska Junk also made very large advances to enterprises in which members of the Wolf and

Schnitzer families were interested. . . . The partnership kept open accounts with all the persons and firms to whom the above mentioned advances were made, charging to such accounts all cash advanced and merchandise furnished, and crediting them with payments in cash or in goods bought by it. (R. 39)

"On June 4, 1941, Morris Schnitzer, son of Sam Schnitzer, organized the Oregon Electric Steel Rolling Mills . . . with an authorized capital of \$250,000.00, represented by 2,500 shares and on that date Morris Schnitzer and Louis Schnitzer, his attorney, subscribed for 1,251 shares and petitioners, Sam Schnitzer and Harry J. Wolf 312½ shares each . . . on February 10, 1942, 1,251 shares were issued to Morris Schnitzer; 312½ to Sam Schnitzer and 312½ to Harry J. Wolf. . . . (R. 40-1)

"No other shares were ever issued although in the beginning the organizers expected to issue more to associate promoters. (R. 48)

"Oregon Steel was organized to erect and operate a rolling mill for the manufacture of steel products. Its stockholders planned to melt down and use scrap metal, which in 1941 was being sold in Portland at \$1.50 to \$2 a ton less than in Seattle, and on the basis of engineers' production estimates expected the earnings eventually to reach \$50,000 or more a month. . . . (R. 41)

"From October 1941 Alaska Junk made numerous advances of cash to Oregon Steel; supplied it with goods of various kinds at cost and paid bills for it. The amounts of cash advanced, the bills paid and value of the goods furnished were charged to its open account with Alaska Junk. . . . All . . . charges were reflected by corresponding credits to the accounts of Alaska Junk . . . on the corporation's books. . . . (R. 42)

". . . in November 1943 they ceased operations, and . . . decided to . . . sell all their shares . . . for one cent a share. Before so doing,

they had the corporation give to Schnitzer Steel Products Co. its promissory note for \$26,829.28 and to Alaska Junk its promissory note for \$427,843.87 . . . equal to the respective credit balances shown on that date in the payees' open accounts with the corporation, . . . (R. 50) . . . Immediately after the sale the purchasers elected new officers and directors, . . . It (Oregon Steel) also gave them . . . its 6 per cent note for \$151,000 . . . secured by a third mortgage on its property . . . (R.51)

"By accepting the \$151,000 note in exchange for the two newly made promissory notes, the five former stockholders . . . failed to recover \$303,-625.90 . . . due from the corporation for their advances on open account, . . . Alaska Junk then charged off \$202,350.70 on its accounts with the corporation as a bad debt. (R. 51-2)

" . . . By 1947 corporate surplus exceeded a million dollars. Since November 26, 1943, and to the present time Oregon Steel has purchased large quantities of scrap from Alaska Junk." (R. 52)

It is difficult to conceive a more clear-cut narration of facts essential to the creation of the debtor-creditor relationship. There is nothing in the sequence of events relating to the transactions which so much as suggests any intention on the part of the petitioners to pay in any part of these advances as capital, except to the extent that entries reflect a charge on the books of Oregon Steel on March 31, 1943 of \$124,900 "to offset balance of stock subscription due against capital Acc. Pay.," and the corresponding entries of July 14, 1943 on Alaska Junk's books reflect contra entries.

It should be noted that the court commented after detailing the entry on Oregon Steel's books (R. 47) "to



offset bal. of stock subscriptions due against Acc. Pay.,' LEAVING A BALANCE OF \$315,095.41 IN THAT ACCOUNT (account payable)." Petitioners had set the amount of debentures and stock they would accept and chose to leave the balance as an account due them. Appropriate contra entries were made on the books of Alaska Junk. Additional shares of Oregon Steel's stock were available, but obviously petitioners had refused to accept more shares than those subscribed for.

These findings clearly demonstrate: the advances were made in accordance with a consistent business policy of long standing for expanding petitioners' regular business of "buying, selling and generally dealing in junk, . . . scrap and other metal products . . ."; a maximum authorized capital for Oregon Steel of \$250,000 fixed upon incorporation; a definite REFUSAL to enlarge it; Alaska Junk's subscription for stock intended to be purchased, made more than four months before any advances were made; settlement of the account by a compromise; the expectation of large profits from Oregon Steel; the eventual outstanding success of the venture and the establishment of a market for Alaska Junk for "LARGE QUANTITIES OF SCRAP" (the very result sought by Alaska Junk); and the final step of writing the loss off as a bad debt.

These and other facts found forcefully corroborate the testimony of petitioners' witnesses. The court should have accorded it full credence, and its failure to do so was plain error. The Trial Court's misstep in reasoning seems to have had its genesis in the fact that it approached the determination of this problem from the



wrong premise. It disregarded the inferences to be drawn from the patent facts pointing toward the EXISTENCE of the debtor-creditor relationship from the day the advances were made, and has required petitioners to assume the burden of overcoming unwarranted inferences and to ESTABLISH THE EXISTENCE of this relationship by an overwhelming preponderance of evidence. The natural, logical inference to be drawn from the facts found is that a loan was intended, but the court obviously closed its eyes to a reasonable construction and chose to wander far afield in search of something to support an ill conceived inference.

In *Kramer v. Gardner*, 104 Minn. 370-3, 116 N.W. 925, 926 (1908), in defining an open account as a debt, the court stated:

“ . . . The expression ‘outstanding and open account’ has a well defined and well-understood meaning. In legal and commercial transactions it is an unsettled debt arising from items of work and labor, goods sold and delivered, and other open transactions, not reduced to writing and subject to future settlement and adjustment.”

The books of ALL PARTIES fully support the contention of petitioners. The accounting followed the nice exactitudes of proper and fully sanctioned business principles. There was not the slightest deviation from the most orthodox standard. Not with any thought of “window dressing” to lay the foundation for a tax deduction, but with one view in mind: to record correctly the actual transactions and in the same manner all previous like transactions had been recorded. This is susceptible

ONLY of the inference the parties INTENDED the advances to constitute debts. All was done that was ever done in business transactions of this kind. Monies were advanced; merchandise was sold at regular prices; invoices were rendered and recorded by Alaska Junk, the vendor, as accounts receivable; the cash and merchandise were received and the obligations were acknowledged and recorded as accounts payable to Alaska Junk by Oregon Steel, the vendee. The transaction was thereby completed and a DEBT created in the manner customary in trade, and consistently followed by Alaska Junk for many years.

All of these facts were found by the court yet it brushed them aside as meaningless. A plain misstep in reasoning.

### III.

#### **The Trial Court's Erroneous Findings and Conclusions**

##### **1. ERRONEOUS INFERENCES DRAWN BY TRIER.**

That the court's reasoning is fallacious is obvious from an analysis of the various items of evidence from which it drew the adverse inferences.

The question is whether the challenged advances created a debt. We say a *prima facie* case is made out by the evidence recording the transactions in question on the books of the various parties involved: the positive testimony of witnesses that the parties intended to cre-

ate a debt: and the recognition and settlement of the debt by the new owners. The witnesses were not impeached, their testimony is not "inherently improbable" and an analysis of the negative evidence upon which the court relied as rebutting the bookkeeping entries and the oral testimony clearly demonstrates they were misconstrued by the court.

(a) *Re Office Memorandum* (R. 43). The court found that on an office memorandum Sam Schnitzer referred to the advances as "contributed capital." There is no such memo in the record and petitioners have no knowledge of such a memo being in existence. Assuming such a memo had been issued, the use of the term had no significance. (See A. W. Groth, R. 490-1, particularly 492.)

"They might have, in fact, been referring to advances by the stockholders or investment in capital stock."

(b) *Re attempts to procure outside capital* (R. 43). No adverse inference may be drawn from attempts to procure outside capital. On the contrary this supports petitioners' position, as it clearly demonstrates a consistent refusal to increase Oregon Steel's capital over \$250,000.00, and at the same time an attempt by Morris to induce others than petitioners to invest in his company. This was a big project for Morris, the promoter, and if he had had the assurance of petitioners that they would agree to an increase in capital he would have been eager to give that assurance to the financial institutions approached.

By refusing to increase the capital stock Morris

deprived himself of an opportunity to obtain outside financing. Commercial Credit and Giannini of Bank of America specifically informed Morris that if he would increase the capital of the corporation they would be interested in assisting in his financing (R. 104, 152-3).

(c) *Re Statement on RFC Application* (R. 43). This statement that additional stock would be taken by Sam Schnitzer and H. Wolf was not made by either of the petitioners but by Morris, the promoter, at which time, October, 1941, he had a controlling interest in Oregon Steel, 1,251 shares, and this statement meant nothing more than that Morris hoped petitioners or others would subscribe for the balance of the authorized capital. Petitioners did eventually take additional stock, which was released by Morris at the time he was called for military duty. This statement in no wise reflected any INTENTION of petitioners.

(d) *Re Guaranty of Note and Agreement to Supply "Additional Working Capital"* (R. 45). Guaranty of the RFC first mortgage note has no bearing upon the issue. The agreement to supply additional monies related to "working capital" only. There is no intimation here of subscribing for additional stock. "Working capital" has no relation to the capital stock of a corporation. Working capital is defined in the Accountants Handbook, Third Edition, 1943, at page 59, as follows:

"Statement of Working Capital.—A statement of working capital (excess of current assets over current liabilities) is a tabulation of current assets and current liabilities designed to emphasize current financial condition. . . ."



The excess of current assets over current liabilities in no sense tends to "enlarge stock investment." Working capital fluctuates daily, varying with the ratio of cash, accounts receivable, inventory and other current assets to notes, accounts and other obligations payable "within ONE YEAR," while stock investment connotes a corporation's permanent investment, which remains constant throughout each year unless additional capital stock is issued or there are additions to surplus, either earned or paid in.

(e) *Re Instrument Dated December 29, 1941 (apparently 1942)* (Resp. Ex. R (R. 45)). Obviously this statement, Respondent's Exhibit R, was prepared by RFC, was presented to the parties and signatures demanded. While it refers to Alaska Junk as having contributed as a capital investment \$299,069.70, reference to testimony of A. W. Groth (R. 492) where he states:

"They might have, in fact, been referring to advances by the stockholders or investment in capital stock."

shows the use of words was not significant. It also shows RFC left open to petitioners the privilege of receiving additional debenture notes, which notes unquestionably are debts. This agreement also states that Alaska Junk "*has contributed* as capital investment, etc." This statement is in the past tense and refers only to advances made up to that time. Alaska Junk accepted stock of \$125,000.00 and received debenture notes of \$174,000.00. These two items total \$299,000.00, which is the amount of Alaska Junk's advance in even thousands, the \$69.70 having been omitted for convenience.

The last paragraph of this agreement reads:



"This agreement is given for the purpose of inducing RFC to disburse said loan, and in consideration of the disbursement thereof in whole or in part."

Respondent's Exhibits X, Y and Z, representing the financial statements supplied by Oregon Steel, all show the advances as a liability to the stockholders, and, in no sense, indicate that they are intended to represent capital investments.

Attention is also called to Exhibit 65, showing the classification of Alaska Junk's account with Oregon Steel, furnished as follows:

"SUMMARY OF ALASKA JUNK COMPANY ACCOUNT  
WITH OREGON ELECTRIC STEEL ROLLING MILLS

	Cash Advance Debited	Bills Paid, Etc. Debited	Merchandise Furnished Debited	Cash Receipts (Credited)	Debit Balance
ct. 22, 1941 to					
Nov. 30, 1942	\$ 42,600.00	\$137,259.04	\$122,823.07	\$ (1,000.00)	\$301,682.
ec. 1, 1942 to					
Nov. 25, 1943	285,270.23	29,081.12	224,518.55	(113,519.88)	425,350.
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
	\$327,870.23	\$166,340.16	\$347,341.62	\$(114,519.88)	\$727,032.
educt—	<hr/>	<hr/>	<hr/>	<hr/>	
Stock				\$124,900.00	
Debentures				174,000.00	298,900.
				<hr/>	<hr/>
alance Nov. 25, 1943					\$428,132.1

It will be noted that merchandise furnished is debited with \$347,341.62 and credited with repayments thereon of \$114,519.88. This account represented merchandise sold to Oregon Steel at regular prices (R. 95, 198, 371) (contrary to the court's findings) and upon which in the ordinary course of business Alaska Junk realized

and reported as taxable income the profits. As to this particular item the transaction is identical with an account created by any merchant selling its goods on open account.

Another important fact in connection with the RFC program leaning in petitioners' direction is the standby agreement required (Resp. Ex. C), dated December 26, 1942 and designating Alaska Junk and Morris as "Standby Creditors." This agreement is in the usual form provided by RFC. Among other things it provides for limiting salaries of "standby creditors"; that it shall remain in force until the RFC loan is repaid; and in paragraph No. 2.

"Without the prior written consent of RFC, no standby creditor will take any action to assert, collect, or enforce all or any part of the claim."

Also respondent's Exhibit D, headed "Standby Agreement", refers to Alaska Junk as a "standby creditor" and states "with respect to the indebtedness owing by the borrower (Oregon Steel) to the 'standby creditor' ", Alaska Junk would not attempt to enforce payment of said indebtedness until RFC had been repaid in full.

Here RFC specifically recognizes the petitioners as creditors and the signing of these standby agreements in no wise affects the rights of these creditors to share upon liquidation as a general creditor.

The true intent of RFC with reference to the advances to Oregon Steel is clarified by Exhibit S, which is headed:

## “AGREEMENT AS TO LOANS TO OREGON STEEL BY ITS STOCKHOLDERS”

This heading indicates that RFC considered, at least, some of the advances as “loans,” and also an indiscriminate use of the term capital investment.

Furthermore, the acceptance of debenture notes instead of stock in the face of availability of additional Oregon Steel shares clearly shows the fixed purpose (intent) of avoiding an additional capital investment in that company.

(f) *Re Agreement to Share Loss One-Third-Two-Thirds* (R. 48). No adverse inference may be drawn from this agreement. The advances were not in proportion to stock holdings at any time. From June 12, 1941 to March 11, 1943 Morris was in control of the corporation by reason of his being the promoter and owner of 1,251 shares (R. 41-47) and it was during this period that Alaska Junk made the major portion of advances (Ex. 26). At the time the debt was compromised Oregon Steel owed Alaska Junk \$428,132.13 and Morris \$26,493.77, total \$454,625.90 (R. 50). Of the \$151,000.00 note given in settlement Alaska Junk received \$142,200.33 and Morris \$8,799.67 (R. 392). Thus the settlement was based upon Oregon Steel's obligation to the respective creditors and not in proportion to stock holdings of one-third and two-thirds.

At the time the stock was originally subscribed for and during which the major amount of the advances was made there was no expectation of a loss. In fact, as the court found (R. 41):

"Oregon Steel was organized to erect and operate a rolling mill for the manufacture of steel products. Its stockholders planned to melt down and use scrap metal, which in 1941 was being sold in Portland at \$1.50 to \$2.00 a ton less than in Seattle, and on the basis of engineers' production estimates expected the earnings eventually to reach \$50,000.00 or more a month."

but the picture changed drastically in 1943. Morris was being inducted into the armed forces. The project was his, the business was being deprived of his energy and knowledge and since Alaska Junk had been drawn into it by Morris, it was only natural that petitioner, Wolf, particularly, would insist upon Morris sharing his portion of Alaska's losses, if any. But this agreement was not a primary obligation. It was only a guaranty, and did not change the obligation of Oregon Steel to Alaska and did not alter the position of Alaska Junk as a general creditor.

From journal entry (R. 52), it may be deduced that of the note of \$151,000.00 given by the new owners of Oregon Steel, Alaska Junk received \$142,200.33, representing 94.1724% of the total of the \$151,000.00, while Morris received only 5.8276% of this note.

Morris Schnitzer's interest in two mortgage notes (R. 52)	\$ 83,799.67
Less his part of debenture notes for \$249,000.00 (R. 46)	75,000.00
	<hr/>
Balance	\$ 8,799.67
Total of third mortgage note received	151,000.00
	<hr/>
Balance received by Alaska Junk	\$142,200.33
Percentage of note received by Alaska Junk, $\$142,200.33 \div \$151,000.00 = 94.1724\%$	



Morris, owner of one-third of stock Oregon Steel, received from the third mortgage note:

Total third mortgage note	\$151,000.00
Received by Alaska Junk	142,200.33
<hr/>	
Balance received by Morris Schnitzer	\$ 8,799.67
Percentage of account recovered,	
$\$8,799.67 \div \$151,000.00 = 5.8276\%$	

Thus the note was divided among the creditors in proportion to their advances and the court's reference to the relationship of the advances to the stock ownership is without merit.

(g) *Re Failure to Designate Use of Advances* (R. 67). The court complains that since no advance, whether by cash payment, materials supplied or discharge of the corporation's bills, was specifically designated as made in satisfaction of stock subscription, in payment for bonds or as a loan, this was a departure from essential form.

The charges to Oregon Steel were made from day to day, and since it was the purpose from the inception that all the items create debts until otherwise designated, the proper inference to be drawn from the books of account is that the parties intended to create a debt for the ENTIRE amount, unless otherwise designated.

This is fully borne out by the fact that only the amount of stock issued to Alaska Junk was charged to this account. This is also true with respect to the portion of the debenture notes accepted by Alaska Junk. These entries did specifically designate the amounts intended to be treated other than as an account.



Also directly in point is the testimony of Leon D. Margosian, a certified public accountant and the accountant for Oregon Steel, which shows conclusively how the funds were intended to be applied.

He testified (R. 452):

" . . . These vouchers or invoices from Alaska Junk Company came to Oregon Steel in the same manner as all other vendors' invoices; we processed them in exactly the same way; we presented them to the Reconstruction Finance Corporation for payment along with other regular invoices; some of them were approved and paid. Those that were not approved and paid, we showed in accounts payable. . . ."

(R. 453):

"Q. What is the basis for the statement?

A. I was instructed by the owners of the firm and by Mr. Riley, their deceased accountant, that after my entry for the stock issued and the debentures had been placed on the books, all other amounts would be current and would be paid either out of the RFC funds or operating profits."

In spite of this positive testimony, no reference to which was made in the court's findings, it concluded there was no specific designation for the use of the funds. This testimony clearly points up the court's misconception of the facts.

(h) *Re Letter Morris Schnitzer March 18, 1943.* (Resp. Ex. AA) (R. 48). The court in referring to letter of Morris Schnitzer to RFC under date of March 18, 1943 and the statement therein contained "never intended to pay in over \$500,000.00 . . . as our share of invested capital" views this document in the wrong

light. Again the use of the term "invested capital" is not significant. In the last paragraph of this letter to RFC in reference to their loan Morris stated:

"Your share of the INVESTMENT here is guaranteed."

Also Morris explained this language (R. 407-8) as meaning a maximum capital of \$250,000.00, \$150,000.00 "working capital" and raw materials to help operate the plant.

(i) *Alaska Junk's Closing Entry* (R. 52). The books of account which were consistently maintained by Alaska Junk and Oregon Steel spell out the only proper conclusion concerning the advances of cash, goods sold and bills paid, and that is, these advances were intended to be and were debts. The force of this evidence is not dissipated, as the Tax Court assumed it was, by the closing entry partially quoted in its opinion. The Tax Court overlooked the fact that this entry covered "investment *and* account" of Alaska Junk. The matter was stated conjunctively. Far from being an indiscriminate lumping, this entry preserved the identity of each segment of the advances. It recorded not only "investment" but *also* the "open account."

Furthermore, the entry as quoted does not give a complete picture, in that it fails to show what a subsequent entry did with the loss there computed. Following the quoted entry the Tax Court paraphrased the subsequent entry into insignificance (R. 52). That entry actually read:

"To Transfer Balance of Account Lost in Settlement

of Account to Bad Accounts." (Exs. 6 and 26)

This demonstrates beyond contradiction that the entry quoted by the Tax Court was no more than the book-keeper's summary of the various amounts which had been paid for stock and debentures and by way of extensions of credit to Oregon Steel. And it is unmistakably true that the purpose disclosed by both entries was to settle the loss sustained on the open account in accordance with the guaranty agreement.

The conclusion of the Tax Court with respect to this entry that "all advances, whether attributed to stocks, bonds, or *loans*" were "indiscriminately grouped for arriving at a settlement" is completely inconsistent with its finding that:

"In connection with the bond issue and stock transfer Morris Schnitzer orally agreed with Sam and Rose Schnitzer and Harry J. and Jennie Wolf that he would bear one-third of any loss that might result from the *total amounts advanced and to be advanced* by all five to the corporation, *over and above the advances credited to stock subscriptions.*" (Italics added) (R. 48)

That the Tax Court classified all advances as being "attributable to stocks, bonds or *loans*" shows that it recognized the \$202,350.60 constituted a loan or debt.

The Tax Court discounted the general importance and weight to be given book entries and in the same breath admitted being completely swayed by this one; this demonstrates it reached its result despite the evidence and its findings.

None of the evidence relied on by the Court supports the inferences drawn by it.

## 2. THE TRIER'S ERRORS OF LAW.

Because of the court's erroneous understanding of the law, it rested its ultimate findings on facts which have little legal significance.

### (a) *Parties' Formal Declarations.*

At the outset the Court stated a rule for interpretation of facts as follows:

“ . . . the parties' formal designations of the advances are not conclusive . . . but *must yield* to 'facts which even *indirectly* may give rise to inferences contradicting' them. *Cohen v. Commissioner*, 148 F. 2d 336 (C.C.A. 2d, 1945).” (R. 64; Italics inserted)

Petitioners submit this is not good law. In all lawsuits contradictory inferences may be drawn. But this is not to say such inferences control the result, nor that proved facts “must yield” to these inferences. An accurate statement of the rule is that in some circumstances other facts “may yield” to these inferences. Nor did the Court correctly quote the Court of Appeals in *Cohen v. Commissioner*, 148 F. 2d 336 (C.C.A. 2d, 1945). That court did not say that the facts “must yield” to conflicting inferences. It stated only that the uncontradicted witness *rule* must yield to contradictory inferences.

As a consequence of its adherence to this fallacious view of the law, the Tax Court misjudged the facts and their weight. Accordingly, its ultimate finding is no more than an erroneous view of the facts.



(b) *Use Made of Advances.*

The Tax Court also placed emphasis on the fact that the advances had been invested in permanent assets. Its view was that the use to which funds are put by the corporation determines the character of the advances. It adopted a standard in direct conflict with the *intent* standard, which this court (9th Circuit) has stressed. Its view was that, regardless of the intent with which the funds are advanced, the corporation's use of those funds determines whether they are capital or debt. According to this theory, in *Joseph B. Thomas*, 2 T.C. 193 (1943) the Tax Court should have held the advances were debts instead of capital, because permanent assets were not acquired. Likewise, bondholders of railroads and industrial concerns must really be stockholders.

The money borrowed from RFC, bank loans, and accounts payable of over \$190,000.00 to outside persons went into permanent assets. Those funds were unquestionably loans. Obviously, this is no criterion, and reliance on this mistaken notion warped the view which otherwise would have been taken of the facts.

(c) *Repayment from Earnings.*

Another error of law was the view that if the corporation had paid off the advances from earnings, such payment would have been a dividend distribution on risked capital. Repayment of debts will always be made from earning unless the debtor is in such hopeless financial straits that it has no earnings and must make payments by depleting its available assets. Surely the Tax Court would not suggest as a rule of law that loans could be made only to the hopelessly insolvent. This is



contrary to established legal doctrine. *American Cigar Co. v. Commissioner*, 66 F. 2d 425 (C.C.A. 2d, 1933). The reasonable expectations are that debts and interest charges on debts will be repaid from earnings. See *Wilshire & Western Sandwiches, Inc. v. Commissioner*, 175 F. 2d 718 (C.C.A. 9th, 1949), where the creditors expected to be and were repaid from earnings, and this court held such facts consistent with a valid debtor-creditor relationship.

(d) *Adequacy of Corporate Capital.*

Another failure of the court to accredit the facts with their plain import resulted from complete reliance on the doctrine of "adequacy of corporation capital previously invested" as an indicium of the intent with which advances are made by stockholders to corporations, and reliance upon this doctrine gave the court a distorted impression of the facts. There are no judicial precedents supporting this doctrine as a test in determining the issue involved. The courts have always been concerned with the "intent" of the parties. The court here outwardly professed a similar concern when it enumerated various evidentiary factors which go to prove intent, but the inclusion of the adequacy factor shows its inclination to disregard the overbearing weight of evidence because of its commitment to this erroneous notion.

The decision of this court in *Maloney v. Spencer*, 172 F. 2d 638 (C.C.A. 9th, 1949), is proof enough of this. In that case the only capital of two food packing corporations was growers' contracts of \$10,000 and

\$5,000, respectively, and the sole stockholder had open account balances with the corporations of \$33,966.02 and \$61,115.48, respectively; yet this court held both accounts to be debts.

Also see *Cleveland Adolph Mayer Realty Corporation*, 6 T.C. 730 (1946), reversed on another point 160 F. 2d 1012 (C.C.A. 6th, 1947), wherein the stockholders of one corporation exchanged their stock therein for stock of \$600 and debentures of \$210,000 of another corporation. The court held the debentures constituted an indebtedness and the interest thereon deductible.

In *Fairbanks, Morse & Co. v. Harrison*, 63 F. Supp. 495 (Ill., 1945), plaintiff corporation purchased all the stock of another corporation for \$7,110 and thereafter advanced it funds on open account, balance in which reached \$796,056.17. Plaintiff claimed a bad debt loss of \$128,466.63, and the court allowed it.

In *Glenmore Distilleries Co.*, 47 B.T.A. 213 (1942), the taxpayer owned all the subsidiary corporation's stock in the amount of \$1,000.00. The taxpayer charged the subsidiary in an open account with merchandise and expenses paid, totaling \$131,457.72. In liquidation a loss of \$80,810.56 was sustained. The Commissioner contended the corporate capital was inadequate. Nevertheless, the Tax Court held the loss was deductible as a bad debt.

Similar is the leading case of *Edward Katzinger Co.*, 44 B.T.A. 533 (1941), where petitioner owned all the subsidiary's capital stock of \$1,000.00. After advancing the subsidiary hundreds of thousands of dollars on open

account, it was liquidated with a loss of \$28,950.06. The Tax Court found that the subsidiary's capital was "insufficient to enable it to carry on its business"; and although the Commissioner made a contention concerning "adequacy of corporate capital", the Tax Court held that petitioner's loss was a bad debt, saying:

"The respondent argues that all of the funds advanced by the petitioner must be regarded as additional capital contributions since *Bruce-Hunt had to have more than \$1,000 with which to conduct its operations . . . the argument fails completely, insofar as it relates to the advances, by reason of the finding that those advances were loans.*" (Italics supplied)

In the case at bar the court used this erroneous doctrine as its major argument to sustain the holding reached, placing the greatest emphasis on the point of "adequacy".

Even though the court's construction of the law on this point were correct, its conclusion based upon the facts would still be erroneous. By its own finding Oregon Steel made a success with its paid-in capital of \$187,800.00. After detailing the ownership of the stock as it was finally distributed (R. 47), in the last sentence of the first paragraph (R. 48) the court stated:

" . . . No other shares were ever issued although in the beginning the organizers expected to issue more to associate promoters."

Also in the second paragraph (R. 52) the court stated:

" . . . By 1947 corporate surplus exceeded a million dollars. . . ."

Also on this point respondent's witness, E. B. McNaughton, testified regarding the earnings of Oregon Steel (R. 443):

"Q. What was the earned surplus for the year 1946?

A. \$379,568.00."

(R. 444):

"Q. And for the year 1947?

A. \$1,191,501.00."

(R. 446):

"Q. . . . Do you know whether this item of surplus included any items of paid-in surplus? . . .

A. No, it does not."

(R. 447):

"Q. Or paid-in surplus by the stockholder or resulting from any other means?

A. No.

Q. Your answer to the last question means that it does not represent any contributions, but represents earnings of the company?

A. It is the result of the earnings of the company."

This earning record of Oregon Steel fully met the estimates of engineers that the mill would earn \$50,000.00 or more per month (R. 41) and fully justifies Morris' expectations and promises. This record of earnings also completely refutes the court's claim of inadequacy of corporate capital as applied to the instant case.

(e) *INTENT the Established Criterion.*

Another erroneous view of the law is amply shown



by the court's statement on "intent" and the authorities cited (R. 63-4):

" . . . And in deciding whether or not a debtor-creditor relation resulted from advances, the parties' true intent is *relevant*, *Fairbanks, Morse & Co. v. Harrison*, (N. D. Ill.), 63 Fed. Supp. 495; *Edward Katzinger Co., supra*, (44 BTA 533); *Daniel Gimbel*, 36 BTA 539."

The cases cited hold that INTENT is CONTROLLING, and this has been the fixed criterion for determining the classification of advances ever since *Edward Katzinger Co. v. Commissioner*, 44 B.T.A. 533, decided in 1941.

For additional cases supporting the proposition that "intent" is CONTROLLING: *Van Clief v. Helvering*, 135 F. 2d 254, 256; *Valentine E. Macy, Jr.*, 8 T.C.M. 45, 1949 Dec. 16,797 M-CCH-7197; *Edward Katzinger Co.*, 44 B.T.A. 531 (1941); *Fairbanks, Morse & Co. et al. v. Harrison*, 63 Fed. Supp. 495.

This court has also considered the question in two cases: *Maloney v. Spencer*, 172 F. 2d 638, decided February, 1949, and *Wilshire & Western Sandwiches, Inc. v. Commissioner*, 175 F. 2d 718, decided June 23, 1949. In *Maloney v. Spencer* the court stated:

"The sums paid in . . . appear as debts due the taxpayer, both on his books of account and those of the corporations. . . . The question is what was the *taxpayer's intent in agreeing* to pay them. *Van Clief v. Helvering*, 135 Fed. (2d) 254, 256. . . . The *Van Clief* opinion, at page 256, states,

" '*Edward Katzinger Co. v. Commissioner*, 44



BTA 533, 536 (CCH Dec. 11, 823). As said by the Board in the case last cited:

“ “ . . . Advances are an additional contribution of capital if they are *intended to enlarge the stock investment*, but not if they are intended as a loan. *Daniel Gimbel (v. Commissioner)*, 36 BTA 539 (CCH Dec. 9754); *Bernuth-Lembcke Co. (v. Commissioner)*, 17 BTA 599 (CCH Dec. 5452);  
 . . . ” ” ”

Also in *Wilshire & Western Sandwiches, Inc. v. Commissioner, Supra*, the court stated:

“The question presented is: Were certain advances of money made to petitioner by its stockholders loans or contributions to capital?  
 . . . . .

The *intent* of the parties as to the *nature of the transaction controls*.”

As this court stated in *Maloney v. Spencer, Supra*, in determining the same issue:

“The sums paid . . . appear as debts due the taxpayer, both on his books of account and those of the corporations.”

The court found in the case at bar the advances were recorded consistently on the books of both debtor and creditor as accounts payable and accounts receivable respectively from the time created until compromised and charged off.

In the *Wilshire* case the advances under attack were originally credited to capital stock accounts and later transferred to notes payable, lending some color to the capital contribution theory, yet this court reversed the Tax Court. Here, on the other hand, ALL ENTRIES

WERE CONSISTENTLY MADE TO DEBTOR-CREDITOR ACCOUNTS AND THEY SO REMAINED TO THE END. At no time did the petitioners attempt to convert "fish to fowl". This applied not only to the petitioners' and Oregon Steel's books but to the books of the companion company, Schnitzer Steel Products Co. Uniformity throughout. Yet the court said there was no adherence to form.

It is significant to note that from the very beginning the intention of Alaska Junk with respect to capital investment was unequivocally limited. On June 12, 1941 Alaska Junk subscribed for capital stock of Oregon Steel (R. 530; Stip. par. 11; Ex. 3). This subscription was made over four months *prior* to the time that Alaska Junk made its first advances in October (R. 42, Ex. 26). That the stock was subscribed for *prior to the advancement of one penny* by Alaska Junk shows beyond contradiction that their original intention was to limit the amount of capital investment.

The original intent of Alaska Junk, as disclosed by its stock subscription many months prior to the first advance, stamped the advances as a debt.

The primary facts found clearly establish an intention on the part of the petitioners to limit their capital investment by the amount of stock subscribed, and the court was not at liberty to disregard the clear, positive, unequivocal, unimpeached testimony of the witnesses called by the petitioner, none of whom were petitioners, that the petitioners did not intend the advances as capital investments but intended them as debts.

Thus, since the "intent" of the parties in making the payments is "controlling", it is obvious that the court was laboring under a misconception of the applicable law.

(f) *Relation of Advances to Stock Holdings.*

While it is true there is an agreement between Morris and Alaska Junk that losses sustained, if any, should be borne one-third and two-thirds and the stock was owned in these proportions, the advances were not in the same proportion. The settlement made with the new owners was on the basis of Oregon Steel's indebtedness to Morris and to Alaska Junk and not the agreement of the parties. Morris received 4.8276% of the settlement payment and Alaska Junk received 94.1724%, notwithstanding the stock ownership of one-third and two-thirds. The test is the obligation of the debtor to the creditor and not what an outside agreement of guaranty represents. Thus, so far as the debtor is concerned Alaska Junk stood to share in and did share in the settlement in proportion of its actual advances and not upon the basis of its stock ownership.

Even though the advances had been in proportion to stock holdings that would not have been fatal. In *Maloney v. Spencer, supra*, respondent was the sole stockholder and his advances would have of necessity been in proportion to his stock holdings. The court did not consider that that made the advances a contribution to capital.

Also in *Wilshire & Western Sandwiches, Inc. v. Commissioner*, the loans to the corporation were in

proportion to the stock ownership and with respect to that condition this court stated:

“The effect of a lending and investing transaction giving creditors, as stockholders, proprietary interest in proportion to their loans, subjects the transaction to close scrutiny, but does not, as a matter of law, require the transaction to be treated as a stock investment, regardless of intent.”

This but emphasizes the erroneous reasoning of the Tax Court.

#### IV.

#### **Review of the Entire Record to Determine Error**

Although this court concludes the inferences drawn by the trial court are supported by the primary facts FOUND, it must independently construe the entire record and draw therefrom the inferences it fairly induces.

The Supreme Court, in a very recent case (*United States v. U. S. Gypsum Company*, 1948, 333 U.S. 364) has stated the scope of the provisions of the Internal Revenue Code and Rule 52 (a) FRCP as follows:

“It was intended, in all actions tried upon the facts without a jury, to make applicable the then prevailing equity practice. Since judicial review of findings of trial courts does not have the statutory or constitutional limitations on judicial review of findings by administrative agencies or by a jury, this Court may reverse findings of fact by a trial court where ‘clearly erroneous’. . . . A finding is ‘clearly erroneous’ when although there is evidence to support it, the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed.”



In *Grace Bros., Inc. v. Commissioner*, 173 F. 2d 170, this court said in this connection:

“This interpretation is not a new departure. It merely stresses, as courts of appeal (including this court), have done before, that findings are to be given the effect which they formerly had in equity. (Equity Rule 70 $\frac{1}{2}$ ) Citing cases.”

Thus, since the adoption of the FRCP, although due regard shall be given to the opportunity of the trial court to judge of the credibility of witnesses, nevertheless the appellate court may reverse “findings of fact” found by a trial court. We perceive this to mean that although the appellate court will not resolve a conflict in the testimony of witnesses it will review every phase of the record to determine if a mistake has been made by the trier in the inferences he has drawn from the evidence adduced. There is no such conflict for this court to resolve. The Tax Court challenged the testimony “particularly of Morris Schnitzer” only upon the fallacious reasoning that it “is INTELLIGIBLE only as showing an agreement about mere form”. Pure sophistry.

#### THE RECORD.

The credibility of petitioners' witnesses stands unchallenged. No attempt was made to establish their standing as to truth and veracity. That was unnecessary, but respondent's witnesses VOLUNTEERED testimony on that point. While respondent was endeavoring to induce his witnesses to testify that Morris Schnitzer or petitioners had made statements which



rebutted testimony that petitioners did not intend to invest more than \$125,000.00 in the capital of Oregon Steel, they volunteered testimony that petitioners were highly regarded by the officers of The First National Bank of Portland (R. 441, 489 and 496, quoted pp. 12, 13, Br.).

Mr. Groth's testimony included the entire Schnitzer and Wolf families, thereby including all of the witnesses who testified as to what amount petitioners intended to invest in Oregon Steel stock.

Notwithstanding this background of credibility the court stated (R. 66):

“ . . . The testimony . . . is intelligible only as showing an agreement about mere form.”

The court did not challenge the “credibility” of the witnesses but, rather, interpreted their testimony upon the basis of a preconceived notion of “intelligibility” as related to “form”. It was saying “I believe the witnesses were telling the truth. However, I believe they meant to say petitioners never intended to put into Oregon Steel any more ‘capital’ as ‘capital’, but they did intend to put in more ‘capital’ as ‘debts’. I don’t believe they were lying. They just didn’t understand the difference in the ‘form’.” Morris’ consistent refusal to increase the capital of Oregon Steel shows he did understand the distinction.

Nothing appears in the record which in any particular tends to impeach the positive testimony of the witnesses, and nothing in the court’s findings tends to do so.

Morris was not a PETITIONER; as he was promoting Oregon Steel, his brain-child, and was most anxious to successfully launch it, his natural inclination would be to do everything possible to meet the requirements of RFC and everyone else to obtain sufficient funds to get the operation under way, yet he steadfastly represented to everyone he approached that the "MAXIMUM CAPITAL" was to be \$250,000. When he was called into service early in 1943, he became aware he could not put in more than \$62,500 and that Alaska Junk WOULD NOT put in more than \$125,000; he had agreed to reserve stock for Rosenbaum on the basis of \$250,000 capitalization and wanted some for a corporate manager. Although he was advised by various concerns that if he would increase the company's capital, loans would be made, he consistently refused to do so. This testimony has added weight because it expresses the attitude of a witness other than petitioners. Because it was his project, it was to his interest to INDUCE Alaska Junk to subscribe for more stock, if that had been possible. Sam Schnitzer was his father and it would have been natural for him to "go the limit" for his son, but Wolf was absolutely opposed to taking more than \$125,000 of stock on behalf of petitioners. None of the witnesses except Monte L. Wolf were petitioners in this proceeding and their testimony was not subject to being colored by self interest.

For the court's convenience the testimony of witnesses on petitioners' intent is summarized:

Morris Schnitzer:

- R. 83 I subscribed for 1,251 shares of Oregon Electric Steel stock because I wanted to have control of the corporation.
- R. 87 . . . this plan was promoted on my idea. I started working on it in 1941, at which time costs were very much lower than they were in later years. We made three different engineering reports and each time each report was a little higher. We never intended to invest so much capital.
- R. 88 I had to spend two years in Washington, D. C. trying to get money, but the amount of capital that we could have put in has never been altered. I don't think that we made any statement anywhere that we ever intended to put in over \$187,000.00 capital stock; . . . we didn't want to put in any more money than we had to.
- R. 89 Mr. Wolf never wanted to put in any more than \$125,000 towards capital.

At the time the company was formed we had a man in New York by the name of Mr. Rosenbaum who was given money for helping us and he was to be given  $12\frac{1}{2}\%$  of the company's stock for his services. We had to keep some open for him and we wanted to have Mr. L. G. Knight come in with an interest in stock and operate the company.

- R. 97 But he (Mr. Rosenbaum) was in Portland in conjunction (R. 98) of setting up the capital stock of Oregon Electric Steel Rolling Mills and he recommended a capitalization of \$250,000.00.
- R. 104 I definitely told Commercial Credit Company that we were limited to the \$250,000.00 capital which had been authorized. We told them it would be a maximum capital of \$250,000.00.
- R. 107 The McDonald report contained a statement that the maximum cost of the mill would be around \$700,000.00 and our maximum capital

was to be \$250,000.00 that we would invest.

- R. 108 We would ask for \$450,000 or \$500,000 loan from the RFC and \$250,000 capital (to make up \$700,000).
- R. 109 We told McDonald Engineering Company it was our intention to authorize stock of only \$250,000.
- R. 139 The reason I figured the \$250,000 for authorized capital was because in our original estimates it would come to about \$700,000.00; with a loan intended to be some \$400,000.00 to \$450,000.00 and \$250,000.00 of our own.
- R. 140 We asked Dulien Steel Products, Jack Barde of Barde Steel Company and Sid Woodbury of Woodbury Steel Co. to buy stock with two things in mind; first, to get some capital and to get them as steel jobbers.
- R. 141 It was not only a question of getting more capital but to get more buyers and consumers and with the added prestige we thought that their names would help us.
- R. 407 The original intention of the \$500,000 was a maximum of \$250,000 in capital stock, and we agreed in our pro forma statement to advance \$150,000 in working capital and raw materials to help operate the plant.
- R. 408 I did not expect Alaska Junk to put in any part of the additional capital that went into Oregon Steel beyond the amount they ultimately subscribed for.

Manuel Schnitzer:

- R. 184 I discussed our company's financial affairs with our accountants quite often, and depended upon them for technical advice; they advised me that (\$125,000.00) (R. 182-185) was the MAXIMUM that we could afford to put into the company.



R. 187 Mr. Wolf always maintained that he would not put in any more than \$125,000.00 on behalf of Alaska Junk company partners, and they agreed not to put in over \$125,000.00.

R. 250 On cross examination: I didn't say we couldn't afford the loss (\$125,000.00). We could not afford to invest in Oregon Steel Rolling Mills more than \$125,000.00.

M. R. Schnitzer (accountant for Alaska Junk Company):

R. 311 We were agreed that the Alaska Junk could afford some \$62,500.00 and later again the question came up as to whether we could afford \$125,000.00 rather than \$62,500.00, and I suggested that if they went beyond \$125,000.00 and tied it up in non liquid form that they might jeopardize the credit of Alaska Junk and thereby their own safety.

R. 312 They owed the bank between \$200,000.00 and \$225,000.00 and private individuals between \$35,000.00 and \$40,000.00 and liquid accounts receivable of approximately \$170,000.00 or \$180,000.00.

R. 319 I heard Mr. Wolf remark about the investment that Alaska Junk would make in Oregon Steel. Under the original plan he told me that the commitments of Alaska Junk were \$62,500.00, and although he was not too happy about it (R. 320) he said he would go on behalf of Alaska Junk to \$125,000.00, *but that was all*;

Monte L. Wolf:

R. 372 My father and mother had agreed with Mr. Schnitzer and the Schnitzer family that, as far as the Alaska Junk Company was concerned, all they wished and saw clear to invest in the Steel Mill was \$62,500.00. My father said he



did not want to put any more in stock, but after discussing the matter mother and father agreed to take part of the shares of Morris Schnitzer on behalf of Alaska Junk.

- R. 374 It was never intended to put in any more on the part of Alaska Junk Company than their final investment in the capital stock of the Oregon Steel.

Leon D. Margosian:

- R. 452 . . . These vouchers or invoices from Alaska Junk Company came to Oregon Steel in the same manner as all other vendors' invoices; we processed them in exactly the same way; we presented them to the Reconstruction Finance Corporation for payment along with other regular invoices; some of them were approved and paid. Those that were not approved and paid, we showed in accounts payable.

- R. 453 Q. What is the basis for the statement?

A. I was instructed by the owners of the firm and by Mr. Riley, their deceased accountant, that after my entry for the stock issued and the debentures had been placed on the books, all other amounts would be current and would be paid either out of the RFC funds or operating profits.

The foregoing testimony was not weakened on cross, and there is not a scintilla of contradictory testimony; nor do the documents adverted to by the court, when analyzed in their true light, rebut this testimony; nor is the testimony of petitioners' witnesses "inherently improbable". It is, therefore, plain that a mistake was committed by the trier.

On this point Judge Simon stated in *Lawton v. Commissioner*, 164 F. 2d 385-388 (C.C.A. 6th, 1947):

"We are aware, of course, that the Tax Court is not required, at all events, to believe the testimony of witnesses, or even to accept at face value documents offered in evidence, but it appears to be well settled that the fact finder may not arbitrarily disregard undisputed and uncontradicted testimony of unimpeached persons where he has already found facts which lend a flavor of truthfulness to their assertions. *Hughes v. Commissioner*, 153 F. 2d 712 (5th CCA); *Bardach v. Commissioner*, 90 F. 2d 323, 326 (6th CCA); *Volz v. Treadway and Marlatt*, 59 F. 2d 643 (6th CCA).

This court's position is stated in *Grace Bros., Inc. v. Commissioner*, *supra*, in the following language:

"It is axiomatic that uncontradicted testimony must be followed. (*Chesapeake and Ohio Ry. v. Martin*, 1931, 283 U.S. 209, 216-217; *San Francisco Association for the Blind v. Industrial Aid*, 8 Cir., 1946, 152 Fed. (2d) 532, 536; *Foran v. Commissioner*, 5 Cir., 1948, 165 Fed. (2d) 705.) The only exception to the rule occurs when we are dealing with testimony by witnesses who stand impeached and whose testimony is contradicted by the testimony of others or by physical or other facts actually proved or in the case of testimony which is inherently improbable."

## CONCLUSION

The only reasonable conclusion upon the record is that the controverted advances were intended to be, and were, debts and that the loss therefrom was fully deductible in the year 1943.

The court was not at liberty to disregard the clear, positive, unequivocal and unimpeached testimony that

the petitioners did not intend the advances to be capital investment, but that they intended them to create debts.

The Tax Court's conclusion, therefore, is not justified. The testimony was straight forward, none of the witnesses were petitioners. There has been no claim of sham or tax avoidance. No witnesses called by respondent controverted the testimony, it is not "inherently improbable", and petitioners' course of conduct was consistent with the testimony.

It follows that the decision of the Tax Court was plainly erroneous, should be reversed and judgment entered for petitioners allowing the deduction as a bad debt in 1943.

Respectfully submitted,

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JACOB & BROWN,

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GARTHE BROWN,  
Of Counsel.

## APPENDIX

### Internal Revenue Code:

#### “Sec. 23. DEDUCTION FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

#### (k) Bad Debts. . . . .

(1) General Rule. Debts which become worthless within the taxable year; or (in the discretion of the Commissioner) a reasonable addition to a reserve for bad debts; and when satisfied that a debt is recoverable only in part, the Commissioner may allow such debt, in an amount not in excess of the part charged off within the taxable year, as a deduction. This paragraph shall not apply in the case of a taxpayer, other than a bank, as defined in section 104, with respect to a debt evidenced by a security as defined in paragraph (3) of this subsection. This paragraph shall not apply in the case of a taxpayer, other than a corporation, with respect to a non-business debt, as defined in paragraph (4) of this subsection.

(4) Non-Business Debts. In the case of a taxpayer, other than a corporation, if a non-business debt becomes worthless within the taxable year, the loss resulting therefrom shall be considered a loss from the sale or exchanges during the taxable year, of a capital asset held for not more than 6 months. The term “non-business debt” means a debt other than a debt evidenced by a security as defined in paragraph (3) and other than a debt the loss from the worthlessness of which is incurred in the taxpayer’s trade or business.”

## Treasury Regulation 111:

“Sec. 29.23 (k)-6 Non-Business Bad Debts.—In the case of a taxpayer, other than a corporation, if a non-business bad debt becomes entirely worthless within a taxable year beginning after December 31, 1942, the loss resulting therefrom shall be treated as a loss from the sale or exchange of a capital asset held for not more than six months. Such a loss is subject to the limitations provided in section 117 with respect to gains and losses from the sale and exchange of capital assets. A loss with respect to such a debt will be treated as sustained only if and when the debt has become totally worthless, and no deduction shall be allowed for a non-business debt which is recoverable in part during the taxable year. Nor are the provisions of this subdivision applicable in the case of a loss resulting from a security as defined in section 23 (k) (3). A non-business debt is a debt, other than a debt the loss from the worthlessness of which is incurred in the taxpayer's trade or business and other than a debt evidenced by a security as that term is defined in section 23 (k) (3). The question whether a debt is one the loss from the worthlessness of which is incurred in the taxpayer's trade or business is a question of fact in each particular case. The determination of this question is substantially the same as that which is made for the purpose of ascertaining whether a loss from the type of transaction covered by section 23 (e) is ‘incurred in trade or business’ under paragraph (1) of that section.

The character of the debt for this purpose is not controlled by the circumstances attending its creation or its subsequent acquisition by the taxpayer or by the use to which the borrowed funds are put by the recipient, but is to be determined rather by the relation which the loss resulting from the debt's becoming worthless bears to the



trade or business of the taxpayer. If that relation is a proximate one in the conduct of the trade or business in which the taxpayer is engaged at the time the debt becomes worthless, the debt is not a non-business debt for the purposes of this section.

To illustrate: A, an individual engaged in the grocery business and who makes his income tax returns on the calendar year basis, extends credit on an open account to B in 1941.

(1) In 1942 A sells the business but retains the claim against B. The claim becomes worthless in A's hands in 1943. A's loss is controlled by the non-business debt provisions. While the original consideration was advanced by A in his trade or business, the loss was not sustained as a proximate incident to the conduct of any trade or business in which he was engaged at the time the claim became worthless.

(2) In 1942 A sells the business to C but sells the claim against B to the taxpayer, D. The claim becomes worthless in D's hands in 1943, at a time when D is not engaged in a trade or business incident to the conduct of which a loss from the worthlessness of such a claim would be a proximate result. D's loss is controlled by the non-business debt provisions, even though the original consideration was advanced by A in his trade or business.

(3) In 1942 A dies, leaving the business, including the accounts receivable, to his son, C, the taxpayer. The claim against B becomes worthless in C's hands. C's loss is not controlled by the non-business debt provisions. While C did not advance any consideration for the claim or acquire it in carrying on his trade or business, the loss was sustained as a proximate incident to the

conduct of the trade or business in which he was engaged at the time the debt became worthless.

(4) In 1942 A dies, leaving the business to his son, C, but the claim against B to his son, D, the taxpayer. The claim against B becomes worthless in D's hands in 1943, at a time when D is not engaged in a trade or business incident to the conduct of which a loss from the worthlessness of such a claim would be a proximate result. D's loss is controlled by the non-business debt provisions, even though the original consideration was advanced by A in his trade or business.

(5) In 1942 A dies and while his executor, C, is carrying on the business, the claim against B becomes worthless. The loss sustained by A's estate is not controlled by the non-business debt provisions. While C did not advance any consideration for the claim on behalf of the estate or acquire it in carrying on a trade or business in which the estate was engaged, the loss was sustained as a proximate incident to the conduct of the trade or business in which the estate was engaged at the time the debt became worthless.

(6) In 1942, A, in liquidating the business, attempts to collect B's claim but finds that it has become worthless. A's loss is not controlled by the non-business debt provisions, since a loss incurred in liquidating a trade or business is a proximate incident to the conduct thereof.

The provisions of this section with respect to non-business debts are applicable only to taxable years beginning after December 31, 1942."



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In the United States Court of Appeals  
for the Ninth Circuit

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SAM SCHNITZER, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

ESTATE OF HARRY J. WOLF, DECEASED, BY MONTE L. WOLF, ADMINIS-  
TRATOR, DE BONIS NON WITH THE WILL ANNEXED OF SAID  
ESTATE, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

MONTE L. WOLF, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

BLOSSOM M. GOLDSTEIN, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

CHARLOTTE C. COHON, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

ESTATE OF JENNIE WOLF, DECEASED, BY MONTE L. WOLF, ADMINIS-  
TRATOR DE BONIS NON WITH THE WILL ANNEXED OF SAID  
ESTATE, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

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ON PETITIONS FOR REVIEW OF THE DECISIONS OF THE TAX  
COURT OF THE UNITED STATES

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BRIEF FOR THE RESPONDENT

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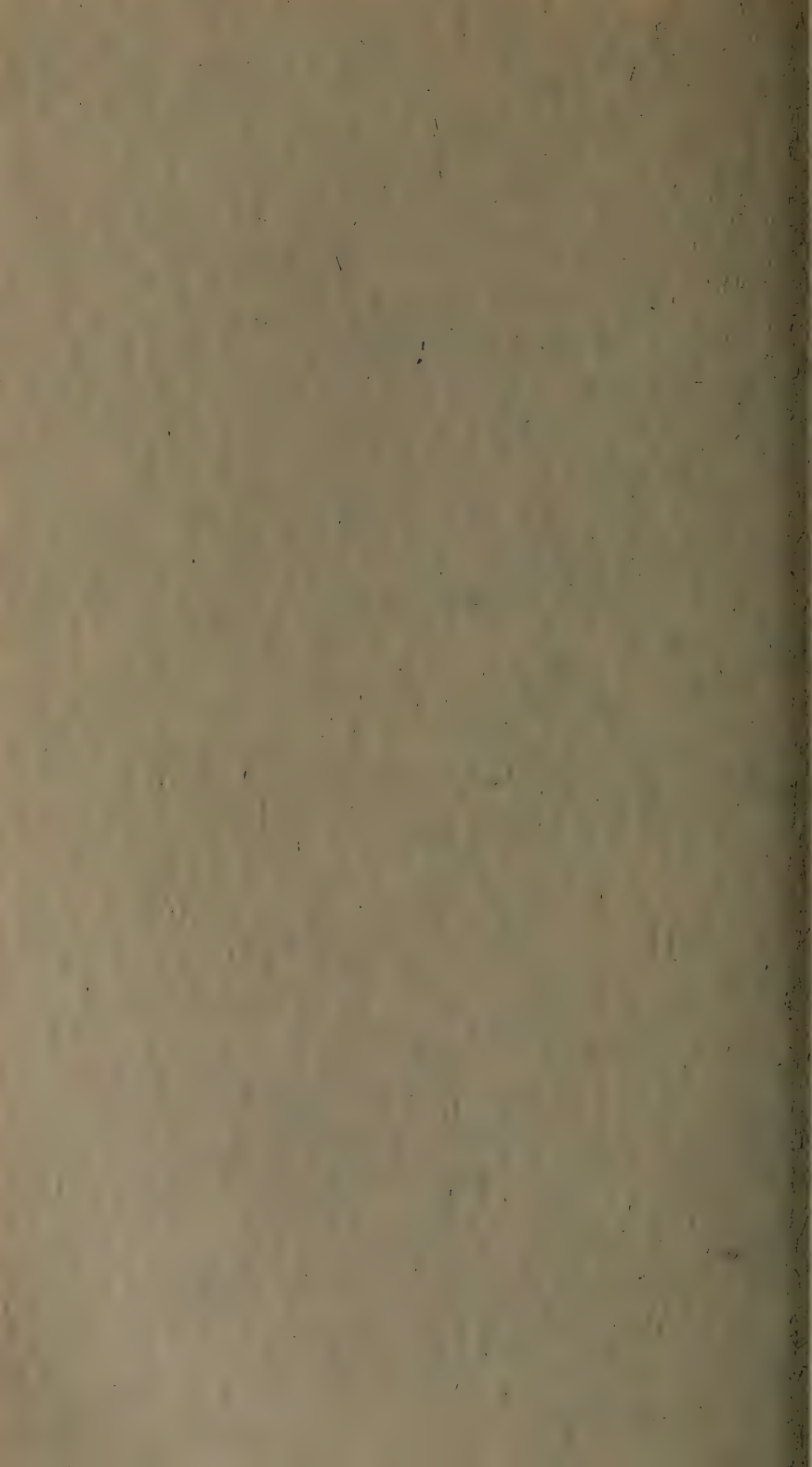
I. Henry Kutz,

*Special Assistants to the  
Attorney General.*

MAY 24 1950

UL P. O'BRIEN,

CLERK





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**In the United States Court of Appeals  
for the Ninth Circuit**

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No. 12,471

SAM SCHNITZER, PETITIONER

*v.*

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

No. 12,472

ESTATE OF HARRY J. WOLF, DECEASED, BY MONTE L. WOLF, ADMINIS-  
TRATOR DE BONIS NON WITH THE WILL ANNEXED OF SAID  
ESTATE, PETITIONER

*v.*

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

No. 12,473

MONTE L. WOLF, PETITIONER

*v.*

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

No. 12,474

BLOSSOM M. GOLDSTEIN, PETITIONER

*v.*

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

No. 12,475

CHARLOTTE C. COHON, PETITIONER

*v.*

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

No. 12,476

ESTATE OF JENNIE WOLF, DECEASED, BY MONTE L. WOLF, ADMINIS-  
TRATOR DE BONIS NON WITH THE WILL ANNEXED OF SAID  
ESTATE, PETITIONER

*v.*

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

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ON PETITIONS FOR REVIEW OF THE DECISIONS OF THE TAX  
COURT OF THE UNITED STATES

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**BRIEF FOR THE RESPONDENT**

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**OPINION BELOW**

The only previous opinion (R. 28-70)<sup>1</sup> is the opinion of the Tax Court, *en banc*, which is reported in 13 T. C. 43.

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<sup>1</sup> Record references are to the record in No. 12,471, *Sam Schnitzer, v. Commissioner*, unless otherwise noted.

## JURISDICTION

The above entitled six cases, consolidated for trial in the Tax Court (R. 548), were by order of this Court consolidated for the purposes of printing the record on appeal, briefing, hearing, argument, and decision (R. 547-549). The petitions for review in each case involve federal income and victory taxes for the year 1943.<sup>2</sup>

The Commissioner of Internal Revenue mailed to each of the taxpayers a notice of deficiency in income and victory tax in the respective amounts below stated for the calendar year ending December 31, 1943, on the dates below stated, as follows:

Docket No.	Taxpayer	Date	Amount of Deficiency	Record References
12,471	Sam Schnitzer.....	3/3/47	\$151,044.45	R. 2-3, 16-20
12,472	Estate of Harry J. Wolf...	3/3/47	151,049.05	R. 2-3, 17-21
12,473	Monte L. Wolf.....	3/4/47	42,273.99	R. 3, 16-19
12,474	Blossom M. Goldstein.....	3/4/47	42,273.99	R. 3, 16-19
12,475	Charlotte C. Cohon.....	3/4/47	42,273.99	R. 2-3, 16-19
12,476	Estate of Jennie Wolf.....	3/3/47	42,273.99	R. 3, 17-20

As appears from these notices of deficiencies, the deficiencies determined against taxpayers Monte L. Wolf, Goldstein and Cohen, respectively, were based upon their liability as transferees of the Estate of Jennie Wolf, Deceased.

Within ninety days thereafter and on the date below stated, each of the above entitled taxpayers filed a petition with the Tax Court for redetermination of the

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<sup>2</sup> No. 12,471, *Schnitzer v. Commissioner*, R. 72-76; No. 12,472, *Estate of Harry J. Wolf, Deceased v. Commissioner*, R. 31-36; No. 12,473, *Monte L. Wolf v. Commissioner*, R. 36-40; No. 12,474, *Goldstein v. Commissioner*, R. 37-42; No. 12,475, *Cohon v. Commissioner*, R. 37-41; No. 12,476, *Estate of Jennie Wolf, Deceased v. Commissioner*, R. 31-36.

deficiency under the provisions of Section 272 of the Internal Revenue Code:

Docket No.	Taxpayer	Date	Record references
12,471	Sam Schnitzer.....	5/26/47	R. 2-15, 20
12,472	Estate of Harry J. Wolf.....	5/26/47	R. 2-17, 21
12,473	Monte L. Wolf.....	5/29/47	R. 2-15, 19
12,474	Blossom M. Goldstein.....	5/29/47	R. 2-15, 19
12,475	Charlotte C. Cohon.....	5/29/47	R. 2-15, 19
12,476	Estate of Jennie Wolf.....	6/ 2/47	R. 2-16, 20

The final order and decision of the Tax Court was entered in each case on November 9, 1949, determining that there is a deficiency on the part of each of the taxpayers below listed in income and victory tax for the calendar year 1943 in the amounts respectively below stated:

Docket No.	Taxpayer	Amount of deficiency determination	Record references
12,471	Sam Schnitzer.....	\$43,287.42	R. 71
12,472	Estate of Harry J. Wolf.....	43,282.00	R. 30
12,473	Monte L. Wolf.....	42,273.99	R. 35
12,474	Blossom M. Goldstein.....	42,273.99	R. 36
12,475	Charlotte C. Cohon.....	42,273.99	R. 36
12,476	Estate of Jennie Wolf.....	42,273.99	R. 30

The tax liability here involved in the aggregate for all six cases is \$128,843.41, since the maximum total tax liability in the last four cases together is limited to \$42,273.99, taxpayers Monte L. Wolf, Goldstein and Cohon, as set forth *infra*, being liable only as transferees of the Estate of Jennie Wolf.

The case is brought to this Court by petitions for review filed by each taxpayer, respectively, on January 4, 1950:

Docket No.	Taxpayer	Record references
12,471	Sam Schnitzer.....	R. 72-77
12,472	Estate of Harry J. Wolf.....	R. 31-36
12,473	Monte L. Wolf.....	R. 36-41
12,474	Blossom M. Goldstein.....	R. 37-42
12,475	Charlotte C. Cohon.....	R. 37-42
12,476	Estate of Jennie Wolf.....	R. 31-37

within three months after the Tax Court's decision was rendered, pursuant to the provisions of Section 1141(a)



of the Internal Revenue Code, as amended by Section 36 of the Act of June 25, 1948, and Section 1142 of the Internal Revenue Code.

#### QUESTIONS PRESENTED

1. Whether or not the Tax Court was clearly erroneous in concluding that advances in the amount of \$202,350 which taxpayers (or their transferor) made to a corporation, of which they were stockholders, constituted capital contributions and not loans and, hence, not deductible, as bad debts within the meaning of Section 23(k)(1) of the Internal Revenue Code.

2. In any event, whether or not the loss was incurred in taxpayers' trade or business within the meaning of Section 23(k)(4) of the Internal Revenue Code, and, hence, deductible only at the limited capital loss rates.

#### STATUTE AND REGULATIONS INVOLVED

The statute and Regulations involved will be found in the Appendix, *infra*.

#### STATEMENT

The decision below was reviewed by the entire Tax Court. (R. 70.) Based on the testimony of eleven witnesses, taken before Judge Luther A. Johnson (R. 78-524) in three days of hearing and on documentary evidence, the Tax Court made the following fact findings:

Taxpayer, Sam Schmitzer, and Harry J. Wolf, deceased, residents of Portland, Oregon, in 1942 and 1943 prepared their income tax returns for those years on the cash basis and filed them with the Collector of Internal Revenue for the District of Oregon. Harry J. Wolf died on February 6, 1948, and his son, Monte L. Wolf, is the personal representative of the Estate of Harry J. Wolf, taxpayer in Docket No. 12,472. Monte

L. Wolf is also administrator *de bonis non* with the will annexed of the Estate of Jennie Wolf, deceased, taxpayer in Docket No. 12,476. Jennie Wolf, wife of Harry J. Wolf, died on April 8, 1945, a resident of Portland, and the owner of property in excess of the deficiencies in tax asserted against her. She filed her income tax returns, prepared on the cash basis, for 1942 and 1943 with the Collector of Internal Revenue for the District of Oregon. Monte L. Wolf, Blossom M. Goldstein, and Charlotte C. Cohon, taxpayers in Docket Nos. 12,473, 12,474, and 12,475, also residents of Portland, are children of Harry J. and Jennie Wolf, and received, as distributees of the residue of Jennie Wolf's estate, assets of a fair market value of \$22,923.09, \$23,855.57, and \$24,112.08, respectively. The distribution of these assets left the estate without means to pay taxes, and, as they stipulated (R. 528-529), these taxpayers became thereby liable as transferees for any deficiency in tax of the transferor estate to the extent of the value of property received by each. (R. 32-33.)

During the years 1942 and 1943 Sam Schnitzer and Harry J. Wolf were active in the operation of the Alaska Junk Company (hereinafter called Alaska Junk), a partnership engaged in the business of buying, selling, and generally dealing in junk, pipe, tools, machinery, hardware, scrap, and other metal products at Portland. The books of Alaska Junk were kept on an accrual basis, and partnership returns, prepared on that basis, were filed for that firm in 1942 and 1943 with the Collector of Internal Revenue for the District of Oregon. On these returns Sam Schnitzer and his wife, Rose Schnitzer, and Harry J. Wolf, and his wife, Jennie Wolf, were listed as partners, and a share of profits was reported as distributable to each. (R. 33-34.)

As Alaska Junk expanded its activities and grew in financial strength, it occasionally made loans or

advances to customers in the expectation of maintaining or increasing its trade. These advances were made sometimes when the customer was indebted to it for goods and were charged to his open account. The books indicate such advances aggregating \$1,600 to M. Turn; \$4,479.63 to Munce & Pedrante; \$1,510 to R. Pedrante; \$2,750 to Emil Nyberg; \$4,500 to the Marshfield Bargain House; \$8,000 to the Medford Bargain House, and \$1,971.08 to various others. All of these customers bought 'scrap and sold it to Alaska Junk or hauled scrap for Alaska Junk, and most of the advances were repaid by cash or by credit for scrap supplied. Some were not repaid. (R. 38-39.)

Alaska Junk also made very large advances to enterprises in which members of the Wolf and Schnitzer families were interested. Schnitzer's son, Morris, individually operated a scrap business under the assumed name of Schnitzer Steel Products Company. Between July 1936 and March 1948 Alaska Junk made to him cash advances aggregating \$119,020.99, of which \$17,517.37 was repaid in cash and the rest in scrap. In 1939 Wolf, Schnitzer, and their wives organized the Central Supply Company as a wholesale dealer in plumbing and electric goods. The organizers, in payment for its capital stock, placed \$50,000 to its credit in an account with Alaska Junk, and Alaska Junk thereafter made to it aggregate cash advances of \$15,500, and also sold it goods. Charges to the account have been paid. In 1939 Wolf, Schnitzer, and their wives and Morris Schnitzer incorporated Industrial Air Products Company for the manufacture of oxygen and acetylene. Alaska Junk was charged with the amount of the stock subscription. Thereafter it made cash advances aggregating \$94,427.03, and it sold merchandise to the company. Repayment was made. In 1940 Wolf, Schnitzer, and their wives and one Shea organized the Plumbing & Heating Sales Company. Alaska Junk

advanced the money for its capital and made sales to it and purchases from it. In 1941 Alaska Junk and Dulien Steel Products Company formed the Carlton Coast Railroad Liquidators as a joint venture to acquire and dismantle a logging camp and railroad and to sell the salvaged materials. Alaska Junk advanced \$27,525 for the venture and acquired a 50% participation, and it has received \$134,649.94 from it. The partnership kept open accounts with all the persons and firms to whom the above mentioned advances were made, charging to such accounts all cash advanced and merchandise furnished, and crediting them with payments in cash or in goods bought by it. (R. 39-40.)

On June 4, 1941, Morris Schnitzer, son of Sam Schnitzer, organized the Oregon Electric Steel Rolling Mills (hereinafter usually called Oregon Steel) as an Oregon corporation with an authorized capital of \$250,000, represented by 2,500 shares of stock of a par value of \$100 each. Of the authorized shares, subscription was made for 1,878 shares as follows (R. 40):

	Shares	Par value
Morris Schnitzer.....	1,250	\$125,100
Sam Schnitzer.....	312½	31,250
Harry J. Wolf.....	312½	31,250
Bernard Levin.....	1	100
Louis Schnitzer.....	1	100

On June 12, 1941, 1 share was issued to each of the 5 subscribers; on August 4, 1 share was issued to L. N. Rosenbaum; and on February 10, 1942, 1,251 shares were issued to Morris Schnitzer, 312½ to Sam Schnitzer, and 312½ to Harry J. Wolf. On February 10, 1942, Sam Schnitzer and Wolf surrendered their 312½ share certificates and 4 new certificates for 156¼ shares each were issued to each of them and their wives. There were also changes in the holders of one share. (R. 41.)

Oregon Steel was organized to erect and operate a rolling mill for the manufacture of steel products. Its stockholders planned to melt down and use scrap metal,



which in 1941 was being sold in Portland at \$1.50 to \$2 a ton less than in Seattle, and on the basis of engineers' production estimates they expected the earnings eventually to reach \$50,000 or more a month. Morris Schnitzer, with whom the idea originated, was made president and general manager. He had been engaged for some years in the purchase and sale of new and used iron, steel, tools, and machinery in Portland under the trade name of Schnitzer Steel Products Company, had had considerable experience in salvage enterprises in various parts of the country, and had studied engineering and business administration at the University of Washington. He was active in seeking capital for Oregon Steel, in getting engineering advice and trade information, and in procuring materials and the necessary priorities. He consulted various steel men and jobbers, arranging outlets for prospective products, and made numerous business trips to New York and Washington. He experienced great difficulties in getting the enterprise started, and actual construction of the mill did not begin until November 1942. Sam Schnitzer, the vice president, and Harry J. Wolf, the secretary, also rendered services. The corporation's board of directors was composed of Morris, Sam and Rose Schnitzer, and Harry J. and Jennie Wolf. None of them had had any experience in steel production. (R. 41-42.)

From October 1941 Alaska Junk made numerous advances of cash to Oregon Steel, supplied it with goods of various kinds at cost, and paid bills for it. The amounts of cash advanced, the bills paid, and the value of the goods furnished were charged to its open account with Alaska Junk. As Alaska Junk had less than \$10,000 cash normally on hand, it often secured bank loans to provide cash advances. Morris Schnitzer likewise advanced cash, paid bills, and supplied goods, and these amounts, together with the expenses of his business trips, were charged to the corporation's account



with Schnitzer Steel Products Company. Nearly all of the advances were for plant and equipment, but after operations began \$9,460 in scrap was furnished by Alaska Junk. All of the foregoing charges were reflected by corresponding credits to the accounts of Alaska Junk and Schnitzer Steel Products Company on the corporation's books. On November 30, 1942, the corporation's account with Alaska Junk showed a debit balance of \$299,069.70 and its account with Schnitzer Steel Products Company, a debit balance of \$138,984.11. On an office memorandum Sam Schnitzer referred to these advances as "contributed capital." (R. 42-43.)

During 1941 Morris Schnitzer made numerous attempts to procure outside capital. In June he besought New York investment banking houses to make a public offering of Oregon Steel's stock, but they declined on the grounds that no proper engineering reports had been submitted and the organizers lacked adequate experience. The Commercial Credit Corporation refused to make a loan because they deemed the \$250,000 authorized capital too small. For the same reasons the Bank of America refused a loan in November 1941. The Bank of Portland refused a loan in April 1942, despite oral assurances by the corporation's officers that \$1,000,000 would be invested in the plant and more would be available for working capital. In October 1941 the corporation filed application with the Reconstruction Finance Corporation for a loan of \$600,000 and employed the engineering firm of MacDonald Bros., Inc., to make a survey and report on the necessary investment and probable operating costs. On this application Morris Schnitzer, signing as president, stated that the corporation proposed to expend \$550,000 of the proceeds on buildings and equipment and \$50,000 on raw materials, brick, manganese, scrap, etc. He estimated that the plant would cost \$890,000, and stated that capital was then \$187,700, but added:

“We expect to increase the capital of this corporation shortly. Additional stock will be taken by S. Schnitzer and J. Wolf to equal that of M. Schnitzer.” On the MacDonald report, filed with the RFC on November 10, 1941, cost of the mill and equipment was put at \$987,035, exclusive of engineering, legal, traveling, and organization expenses. Organization expenses were given as \$65,000. (R. 43-44.)

The RFC was not satisfied with the MacDonald report, and a second was submitted from another engineer, who estimated that the mill would cost \$1,050,000. On April 2, 1942, the executive committee of the RFC approved the loan, subject to listed conditions. After several changes had been made in the conditions, Sam Schnitzer and Wolf, as partners of Alaska Junk, wrote RFC on December 1, 1942, that cost of the mill might exceed \$1,200,000 and that Alaska Junk would furnish any necessary money in excess thereof to complete the project if RFC would lend an additional \$100,000. On December 4, 1942, RFC approved a loan of \$700,000, having received assurance that there had been no change in the borrower's financial condition and business prospects. Oregon Steel gave to the Federal Reserve Bank of San Francisco its 4 per cent promissory note for that amount, dated December 15, 1942, payable within 5 years by monthly installments of \$6,500 from May 1, 1943, and by an additional annual payment sufficient to make all payments equal to 50 per cent of the corporation's net earnings for the preceding year. The note was secured by a duly recorded mortgage on the corporation's real estate and the plant to be constructed and equipped and on its personal property with the exception of cash, receivables, raw materials, and inventories. Effective supervisory powers were given to RFC to enforce current compliance with the terms. (R. 44-45.)

By separate agreement Morris, Sam and Rose Schnitzer, and Harry J. and Jennie Wolf individually

guaranteed repayment of the note and bound themselves to supply "additional working capital" in amounts deemed satisfactory by RFC as long as any part of the loan should remain unpaid. The corporation bound itself to limit officers' annual salaries for such period to a total of \$25,000, and to pay in cash no more than \$15,000. In an instrument of December 29, 1941, the corporation, Morris Schnitzer, and Alaska Junk recited that Morris Schnitzer and Alaska Junk had already contributed \$138,984.11 and \$299,069.70, respectively, in the form of cash or property to the corporation; that (R. 45):

\* \* \* Such contributions by stockholders have, as stated, been as a capital investment, and in no wise as outstanding accounts payable by Borrower, except to the extent that Borrower's debenture notes may be issued for a part of such contributions or capital investment.

The stockholders further agreed that they would receive in payment of "all such capital investments so made" only the common stock or debenture notes of the corporation and the corporation in turn covenanted to make payments in no other way. The corporation further agreed that, as long as any part of the RFC loan should remain unpaid, it would not issue to stockholders any preferred stock or evidence of indebtedness except debentures on a prescribed form "in return for advances made or to be made by them." The prescribed form forbade payment of principal or interest on the debentures until full repayment of the RFC loan. These conditions were observed, but RFC did allow reimbursement for about \$114,519 of subsequent advances for the purchase of mill equipment. (R. 45-46.)

While the final terms of the RFC loan were being arranged, Wolf expressed dissatisfaction because Mor-

ris Schnitzer, holding two-thirds of the corporate stock, had not made a proportionate part of the advances. Costs of the enterprise had already exceeded anticipations, and Morris was financially unable to advance more. The stockholders entered into negotiations among themselves for a more satisfactory distribution of interests. They reached an agreement, and pursuant thereto the corporate directors authorized issuance of debenture bonds for \$250,000 on terms contemplated by the understanding with RFC. On January 12, 1943, it issued such bonds in an aggregate of \$249,000 to its stockholders in the following amounts (R. 46):

Morris Schnitzer .....	\$75,000
Sam Schnitzer .....	44,000
Rose Schnitzer .....	43,000
Harry J. Wolf .....	44,000
Jennie Wolf .....	43,000

These bonds bore 8 per cent interest and were payable within 10 years of issue, but no payment of interest or principal could be made while any balance remained due on the corporation's \$700,000 note to RFC. (R. 47.)

As part of the settlement agreement Morris Schnitzer on March 11, 1943, surrendered 626 of his 1,251 shares of stock. One share was reissued to Monte L. Wolf and the remainder to Sam Schnitzer and wife and Harry J. Wolf and wife, so that the corporation's 1,878 outstanding shares were thereafter held as follows (R. 47):

	Shares		Shares
Morris Schnitzer.....	625	Harry J. Wolf.....	313½
Sam Schnitzer.....	313½	Jennie Wolf.....	312½
Rose Schnitzer.....	312½	Monte Wolf.....	1

By entries of March 31, 1943, the corporation charged the open account of Schnitzer Steel Products Company (Morris Schnitzer) with \$75,000 for "debentures issued" and with \$62,500 "to offset bal. of stock subscriptions due against Acc. Pay.," leaving a credit balance of \$6,638.23 in the account. By entries of the same



date it charged Alaska Junk's open account with \$174,000 "to record debentures issued" and with \$124,900 "to offset bal. of stock subscriptions due against Acc. Pay.," leaving a balance of \$315,095.41 in that account. By entries of July 14, 1943, Alaska Junk credited the corporation's account by corresponding amounts, specifying that the shares and bonds had been issued to Sam and Rose Schnitzer and to Harry J. and Jennie Wolf in the amounts above set forth. No other shares were ever issued, although in the beginning the organizers expected to issue more to associate promoters. (R. 47-48.)

In connection with the bond issue and stock transfer Morris Schnitzer orally agreed with Sam and Rose Schnitzer and Harry J. and Jennie Wolf that he would bear one-third of any loss that might result from the total amounts advanced and to be advanced by all five to the corporation, over and above the advances credited to stock subscriptions. They in turn agreed to bear two-thirds of any such loss. Morris Schnitzer and Alaska Junk continued thereafter to make advances, as before, and these advances were credited to their open accounts with the corporation in the same way as before and charged to the corporation's open accounts with them. (R. 48.)

In asking for larger releases of the authorized loan, Morris Schnitzer on March 18, 1943, wrote RFC that costs were rising and that the stockholders had "in this job over \$700,000 of our own money," but "never originally intended to put in over \* \* \* the \$500,000 we were supposed to put in as our share in the capital investment." In a prior letter of December 23, 1942, he had referred to "additional costs for the extensions and additions" to the plant, suggested in the McKee report to increase production capacity, and requested approval of them. (R. 48-49.)



Construction work on the mill began in November 1942, but building materials were hard to obtain; new machinery was scarce; priorities could not be procured for some requirements; and second-hand equipment and materials had to be used in part. Prices steadily increased. The mill was finally completed in June 1943 at a cost of \$1,400,000, and the melting of scrap into ingot started soon thereafter. About the same time Morris Schnitzer entered the military service, and his brother, Manuel Schnitzer, who had been employed by the corporation since the preceding January, took charge. Manuel was not familiar with steel manufacture; two engineers, successively engaged as managers, proved unsatisfactory; and competent personnel and operators were difficult to find. Manuel made vigorous efforts, however, and rolling operations were begun late in August. But the machinery did not function properly; production was so far behind schedule that many large orders were canceled by customers, principally the United States Government; creditors pressed for the payment of bills; there was a lack of ready cash; and a serious financial crisis developed. In June 1943 the corporation began to get some relatively small loans from banks, secured by its steel inventory and warehouse receipts for scrap. By November 26 these amounted to \$149,499.71. (R. 49.)

The stockholders again tried unsuccessfully to interest outsiders to take a participating interest, and approached the United States Steel Company, Bethlehem Steel Company, Republic Steel Company, Henry Kaiser, and others. But in November 1943 they ceased operations, and on November 26 they decided to withdraw from the enterprise entirely and to sell all their shares to Kenneth E. Hall and A. M. Mears for one cent a share. Before so doing, they had the corporation give to Schnitzer Steel Products Company its promissory note for \$26,829.28 and to Alaska Junk its promissory

note for \$427,843.87. The amounts of these notes were equal to the respective credit balances shown on that date in the payees' open accounts with the corporation, but as later computed such balances were in fact \$26,493.77 and \$428,132.13, respectively. That of Alaska Junk reflected the following aggregate debits and credits (R. 50):

Debits		Credits	
Cash advanced.....	\$327,870.23	Stock.....	\$124,900.00
Bills paid.....	166,340.16	Bonds.....	174,000.00
Goods furnished.....	347,341.62	Repayments.....	114,519.88
Total.....	841,552.01	Total.....	413,419.88

Immediately after the sale the purchasers elected new officers and directors, Mears becoming president. Pursuant to a resolution of the new directors and with the consent of RFC, the corporation gave to Morris, Sam and Rose Schnitzer, and Harry J. and Jennie Wolf its 6 per cent note for \$249,000, payable in annual installments of \$24,900 beginning June 1, 1954, and secured by a second mortgage on the corporation's property. It also gave to them its 6 per cent note for \$151,000, payable in annual installments of \$15,100 beginning June 1, 1954, and secured by a third mortgage on its property. In consideration of these notes the payees surrendered to the corporation the debenture bonds for \$249,000 and the newly made promissory notes for \$26,829.28 and \$427,843.87. (R. 51.)

By accepting the \$151,000 note in exchange for the two newly made promissory notes, the five former stockholders of Oregon Steel failed to recover \$303,625.90 of the total shown due from the corporation for their advances on open account, which at the time showed credit balances aggregating \$454,625.90. Pursuant to his agreement, Morris Schnitzer made reimbursement to the other four in the amount of \$83,581.20 in order to reduce their loss to two-thirds of the total. This settlement was effected by a charge of that amount to

Morris on the books of Alaska Junk and by his later delivery of second mortgage notes on account thereof to Alaska Junk. The charge of \$83,581.20 was explained in the journal as follows (R. 51-52):

To charge Morris Schnitzer with  $\frac{1}{3}$  of total loss in steel mill deal. Total investment and a/c of A. J. Co. 727,032.13; total of Morris Schnitzer 163,993.77 or 891,325.90 for both—Total payment by mrtge 400,000. Total loss 491,325.90. Morris' share of loss  $\frac{1}{3}$  or 163,775.30. His investment and a/c of 163,993.77 less his interest in two mtge notes of \$83,799.67 results in loss of 80,194.10 on the amount he expended plus 83,581.20 due us.

Alaska Junk then charged off \$202,350.60 on its accounts with the corporation as a bad debt. (R. 52.)

On October 3, 1943, the corporation's books indicated an operating loss to date of \$59,562.91. There were small operating losses in 1944 and 1945. For 1946 the books indicate a profit of \$278,196.85 before taxes. By 1947 corporate surplus exceeded a million dollars. Since November 26, 1943, and to the present time Oregon Steel has purchased large quantities of scrap from Alaska Junk. (R. 52.)

Alaska Junk's partnership return for 1942 disclosed net profits of \$236,123.45, of which \$64,030.86 was reported as the distributable share of Sam Schnitzer; a like amount as the share of Harry J. Wolf; and \$54,030.86 as the distributable shares of each of their wives. Each of the four included such share in the income reported on his individual income tax return for 1942. Alaska Junk's partnership return for 1943 disclosed net profits of \$246,055.71, of which \$66,513.92 was reported as the distributable shares of Sam Schnitzer and Harry J. Wolf and \$56,513.93 as the distributable shares of their wives. Each of the four included such share in the income reported on his in-



dividual income and victory tax return for 1943. (R. 52-53.)

In computing the incomes of taxpayer Sam Schnitzer and Harry J. Wolf for 1942 and 1943, the Commissioner denied recognition to the wives as partners for tax purposes, and included half of the partnership's net profits in the income of each of them. On the partnership's return for 1943 a deduction of \$202,350.60 was claimed as a bad debt, represented by Alaska Junk's open account with the corporation. The Commissioner disallowed this deduction. In the event that his failure to recognize Jennie Wolf as a partner should not be sustained, the Commissioner also determined a 1943 deficiency against her estate, computed to reflect her claimed share in the partnership income as recomputed by him.<sup>3</sup> The Commissioner further determined that taxpayers Monte L. Wolfe, Blossom M. Goldstein, and Charlotte C. Cohon are liable for Jennie Wolf's tax deficiency as transferees of her estate. (R. 53.)

On redetermination the Tax Court held that the wives were entitled to recognition as partners of Alaska Junk for tax purposes. (R. 56-61.) The Commissioner has not appealed from this adverse holding of the Tax Court below and the partnership issue is thus not before this Court.

On the other hand, the Tax Court sustained the Commissioner's determination disallowing the deduction, as a bad debt, of \$202,350.60 from Alaska Junk's part-

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<sup>3</sup> For the further information of this Court, the following is quoted from the Commissioner's brief in the Tax Court (p. 56, fn. 12):

Although there is nothing in the record on this point, respondent nevertheless desires to inform the Court that \* \* \*. No deficiency has been asserted against her [Rose Schnitzer, wife of taxpayer Sam Schnitzer] for the reason that she executed a waiver of the statute of limitations thereby permitting an assessment at a future date. No waiver was executed by the Estate of Jennie Wolf.

nership profits for 1943, holding that the advances were contributions to the capital of Oregon Steel, and hence their ensuing worthlessness was not a bad debt. (R. 61-70.) The deficiencies sustained by the Tax Court in the case of each taxpayer are the result of the conclusion of this single issue in favor of the Commissioner.

#### SUMMARY OF ARGUMENT

The statutory grant of the bad debt deduction is premised upon the establishment by a taxpayer of the existence of the "debts" sought to be deducted, and in applying its terms the first consideration is whether a given taxpayer was in fact owed any debt at all. Since the question is one of fact, it is primarily for determination by the trier of the facts, instantly the Tax Court, whose factual findings here sustain the Commissioner's determination and are entitled to finality, unless clearly erroneous. The burden in this Court is upon taxpayers to establish that the finding of the Tax Court, that Oregon Steel was not indebted to them for the amount sought to be deducted, was clearly wrong. Furthermore, since taxpayers base their claim upon a deduction the rule of construction is strict. The bad debt deduction, like other deductions, is a matter of legislative grace and the burden is upon taxpayers to show that the facts bring the case squarely within the terms of the legislative grant. This strict standard is not satisfied by proof of equivocal circumstances. To escape liability taxpayers must show clear indebtedness and, they do not comply with the well settled rule where, as here, reading the evidence most favorably to them they have shown only a hybrid situation.

The record facts substantiate the Tax Court's conclusion of no debt. The testimony upon which taxpayers rely was given by interested or friendly witnesses approximately five years after the events in



issue and was conclusory in character. On the other hand, there were adduced in evidence many contemporaneous record facts and documents inconsistent with the oral conclusions of these witnesses. This testimony as to intent was carefully considered by the Tax Court who saw the witnesses and observed their demeanor, candor and credibility under examination, and also which carefully found and appraised the documentary exhibits and other record facts and inferences arising from such facts. Taxpayers are not entitled, as they appear to think, to come to this Court for what virtually would amount to a trial de novo of such a finding as intent.

The Tax Court, among other things, was warranted in considering that no interest was charged at any time for the alleged loans despite the circumstances that Alaska Junk, the supposed creditor, maintained its books on the accrual basis. With the exception of formal notes given on the very day that they were cancelled and on which taxpayers sold their interest in Oregon Steel to new owners, no notes, certificates or other evidence of debt in any form were ever given by Oregon Steel to taxpayers in recognition of any of the advances, upon which the instant bad debt deduction is founded. A chronological analysis of the undisputed acts and dealings of taxpayers from the organization of Oregon Steel until they sold their interest, during the period of approximately two and one-half years, demonstrates that there is not to be found any contemporaneous clear, unambiguous and binding expression by the stockholders or otherwise that the balance on the open account of Alaska Junk was intended by them to be debt. On the contrary there were numerous contemporary statements and acts of the stockholders inconsistent with claim of debt, which the fact finder, weighing the evidence, was entitled to regard as nulli-

fying the bare and conclusory testimony of intent to loan offered at the hearing.

Moreover, during the entire period under consideration accepted indicia of debt were absent, such as fixed maturity date for payment, agreement on interest rate, accrual of interest, no subordination to creditors, divorce from management, security for payment, written evidence of indebtedness, timely and clear entry in purported creditor's books. In addition, among other criteria, sustaining the Tax Court's conclusion is the significant circumstance that this was a lending and investing transaction under which losses were matched in proportion to stockholding and were actually so computed on the taxpayers' books. Finally the Tax Court was warranted in considering the obviously excessive debt structure as against comparatively nominal stock investment, if taxpayers' claim is to be credited.

The administration of a great revenue system is a practical matter; Congress did not propose to grant deduction to ambiguous transactions, subject to treatment at a taxpayer's option as debt or investment. To expand the meaning of "debts" to include the advances involved in the instant case would, indeed, relax the strict rule of construction, which has obtained in the case of deductions under the various Revenue Acts.

The Tax Court correctly applied the relevant authorities. The primary facts may be undisputed, as substantially they are here, but conflicting inferences may reasonably be drawn from them, and it is the peculiar province of the fact finder to draw such inferences and weigh the evidence in the light of these inferences. It is not enough that an appellate court might give the facts another construction and resolve ambiguities differently. The appellate scope of review, as settled by the highest authority, is not to set aside findings of fact, unless clearly erroneous. Applying these principles

here, it is submitted that the factual conclusion reached by the fact finder, in weighing the evidence and the inferences to be drawn from it and in construing and resolving its ambiguities, was correct and certainly cannot be regarded on review as clearly erroneous.

Furthermore, in any event, should this Court hold, contrary to our contention, that debts did result from the advances, nevertheless they were not business debts and, hence, as provided by Section 23(k)(4) of the Code, are considered as a loss from the sale or exchange of a capital asset held for not more than six months and deductible only at capital loss rates. Certainly, it is not a normal incident of taxpayers' business, which consisted of selling iron and steel scrap or of selling finished steel, to go into the business of manufacturing steel, as taxpayers did.

#### ARGUMENT

#### I

**The Record Amply Sustains the Conclusion of the Tax Court,  
That Oregon Steel Was Not in Fact Indebted to Taxpayers,  
Its Stockholders, in the Amount They Seek to Deduct as a  
Bad Debt**

##### A. *The Issue*

Taxpayers invoke the provisions of Section 23(k)(1) of the Internal Revenue Code (Appendix, *infra*), under which Congress has "allowed" as a deduction from gross income "Debts which become worthless within the taxable year". Taxpayers contend for the deduction in full of the sum of \$202,350, which they claim constituted such a bad debt. On the other hand, the Commissioner treated this amount as a loss in capital investment (R. 61), thus deductible, not in full, but at the lesser capital loss rates. See Internal Revenue Code, Section 117.

Clearly, this statutory grant of the bad debt deduction is premised upon the establishment by a taxpayer of the existence of the "debt" sought to be deducted,



and in applying its terms the first consideration is whether a given taxpayer was *in fact* owed any debt at all. *Bercaw v. Commissioner*, 165 F. 2d 521, 525 (C. A. 4th). Further, as the Tax Court here correctly held, this question is one of fact (R. 63), and thus, as with all factual questions, its solution varies with and depends upon the peculiar circumstances of the individual case. *John Kelley Co. v. Commissioner*, 326 U. S. 521; *Cohen v. Commissioner*, 148 F. 2d 336 (C.A. 2d).

Such fact questions are primarily for determination by the trier of the facts, instantly, the Tax Court, and its factual findings here sustaining the Commissioner's determination are entitled to finality "unless clearly erroneous". Rule 52(a), Federal Rules of Civil Procedure.<sup>4</sup> *Grace Bros. v. Commissioner*, 173 F. 2d 170 (C. A. 9th); *Joe Balestrieri & Co. v. Commissioner*, 177 F. 2d 867 (C. A. 9th); *Smyth v. Commissioner*, (C. A. 9th), decided April 5, 1950 (1950 C.C.H., par. 9267).

Rule 52 (a) further provides: "due regard shall be given to the opportunity of the trial court to judge of the credibility of the witnesses". Here there was substantial oral testimony and the credibility to be afforded to the witnesses, particularly interested witnesses or those closely related to taxpayers, in view of all the circumstances of the case, is for the fact finder who saw and heard them and possessed the opportunity to observe their demeanor upon the stand.

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<sup>4</sup> Internal Revenue Code:

SEC. 1141 [As amended by Section 36 of the Act of June 25, 1948, c. 646, 62 Stat. 869]. COURTS OF REVIEW.

(a) *Jurisdiction*.—The courts of appeals shall have exclusive jurisdiction to review the decisions of the Tax Court, except as provided in Section 1254 of Title 28 of the United States Code, in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury; \* \* \*.

(26 U.S.C. 1946 ed., Supp. II, Sec. 1141)

*Greenfield v. Commissioner*, 165 F. 2d 318 (C.A. 4th); *Katz Underwear Co. v. United States*, 127 F. 2d 965 (C.A. 3d), certiorari denied, 317 U.S. 655; *Grace Bros. v. Commissioner*, *supra*, p. 174; *Joe Balestrieri & Co. v. Commissioner*, *supra*, pp. 873-874.

Moreover, the burden in this Court is upon taxpayers to establish that the finding of the Tax Court, that Oregon Steel was not indebted to them for the amounts sought to be deducted, was clearly wrong. As this Court held in *Grace Bros. v. Commissioner*, *supra*, p. 174:

In giving effect to these norms in a particular case, the burden is upon him who attacks a finding to show that it is clearly wrong. *In re American Mail Line*, 9 Cir., 1940, 115 F. 2d 196, 199; *Wittmayer v. United States*, 9 Cir., 1941, 118 F. 2d 808, 810; *Augustine v. Bowles*, 9 Cir., 1945, 149 F. 2d 93, 96.

Furthermore, an additional burden is incumbent upon taxpayers, both in this Court and below, inherent in the particular statutory foundation of their claim. Taxpayers base their claim upon a deduction and the bad debt deduction, like other deductions, is a matter of legislative grace. The rule of construction is strict. It does not turn upon general equitable considerations; only if there is clear provision therefor can any particular deduction be allowed. *Equitable Society v. Commissioner*, 321 U.S. 560, 564; *New Colonial Co. v. Helvering*, 292 U.S. 435, 440; *Deputy v. duPont*, 308 U.S. 488, 493; *Brown-Rogers-Dixson Co. v. Commissioner*, 122 F. 2d 347, 350 (C. A. 4th); *Pacific Southwest R. Co. v. Commissioner*, 128 F. 2d 815, 817 (C. A. 9th), certiorari denied, 317 U.S. 663. The burden is upon the taxpayers to show that the deduction claimed clearly falls within the terms of the statute, and, thus, includes the burden of proving



that there was an "indebtedness". *Commissioner v. Drovers Journal Pub. Co.*, 135 F. 2d 276, 278, 279 (C. A. 7th). In *White v. Commissioner*, 67 F. 2d 726, 728, this Court said:

It is conceded by appellants, as it must be under the authorities, that no deduction from income can be claimed as a matter of right and whatever deduction may be taken is solely a matter of statutory grant. *Lloyd v. Commissioner* (C.C.A.) 55 F. (2d) 842. *The burden is upon the taxpayer to prove that the facts bring the case squarely within the deduction provisions of the statute.* *Burnet v. Houston*, 283 U.S. 223, 51 S. Ct. 413, 75 L. Ed. 991; *Reinecke v. Spalding*, 280 U.S. 227, 50 S. Ct. 96, 74 L. Ed. 385. (Italics supplied.)

See also to this effect *Interstate Transit Lines v. Commissioner*, 319 U.S. 590, 593, and *Boehm v. Commissioner*, 326 U.S. 287, 294, rehearing denied, 326 U.S. 811.

Applying this principle instantly, the taxing statute allows deduction for bad "debts" and taxpayers who seek to take advantage of the legislative grant must show facts squarely bringing them within its terms. Surely this strict standard is not satisfied by the proof of ambiguous and equivocal circumstances which may be read to point either to investment or to debt. To escape liability taxpayers must show clear indebtedness and they do not comply with this well settled rule, where, as here, the evidence reveals only a hybrid situation, which in their uncontrolled power taxpayers might interpret either way—for stock or for debt—as events transpired and their advantage proved. Certainly, in generously granting the deduction Congress did not intend and the statute should not be misread to subject the amount of his tax liability to the substantially untrammelled control of any taxpayer.

Thus, we submit the Tax Court, applying these standards to the instant record, was entitled to conclude that taxpayers had not clearly shown indebtedness to them from Oregon Steel and had not complied with the strict rule of construction of the congressional grant which they invoke; indeed, the record requires the contrary conclusion, namely, that their advances in issue, as partners in Alaska Junk to Oregon Steel, constituted risk capital and not loans.

*B. The record facts substantiate the Tax Court's conclusion of no debt*

Taxpayers' chief reliance is on the testimony of their witnesses at the hearing, especially Morris Schnitzer, that the shareholders never intended to invest more than \$187,800 in stock. (R. 66.) These witnesses were either interested or close relatives of interested persons, or otherwise closely identified with Alaska Junk. Their testimony (see e.g., the parts selected by taxpayers for quotation in their brief (pp. 54-57)), consists mainly of bare and conclusory statements of intent by Morris Schnitzer or attributed by him and others to Sam Schnitzer and Harry J. Wolf. The latter had died some months prior to the hearing (R. 33), and Sam Schnitzer did not testify.<sup>5</sup>

The testimony, upon which taxpayers rely, was given approximately five years after the events in issue; on the other hand, there were adduced in evidence many contemporaneous record facts and documents inconsistent with the oral conclusions of the witnesses. (R. 64-70.) This testimony as to intent was carefully considered by the Tax Court (R. 66), which saw the witnesses and observed their demeanor, candor and

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<sup>5</sup> A physician called by taxpayers testified that Sam Schnitzer had heart trouble and his appearance as a witness might jeopardize his health. Typewritten transcript of hearing, pp. 519-525.)

credibility under examination, and which also carefully found and appraised the many documentary exhibits and other record facts and inferences arising from such facts. (R. 40-52, 64-70.) On established principles, already adverted to (subpoint A, *supra*), such weighing and analysis of the evidence was properly and primarily within the province of the fact finder. Taxpayers are not entitled, as they appear to think, to come to this Court for what virtually would amount to a trial *de novo* on the record of such a finding as intent. So the Supreme Court recently held, in *United States v. Yellow Cab Co.*, 338 U.S. 338, 340-342, where *inter alia*, it is said (p. 341):

Findings as to the design, motive and *intent* with which men act *depend peculiarly* upon the credit given to witnesses by those who see and hear them. (Italics supplied.)

The Tax Court was warranted on the highest authority to afford little weight to such testimony in conflict with contemporaneous documents. *United States v. Gypsum Co.*, 333 U. S. 364, 396, rehearing denied, 333 U. S. 869.

The Tax Court did not err in declining to accept testimony of interested or friendly witnesses in the nature of general statements, unsupported by contemporary acts and documents, and which in the light of the entire record might reasonably be regarded as inherently improbable. *Greenfield v. Commissioner, supra*; *Grace Bros. v. Commissioner, supra*; *Joe Bales-trieri & Co. v. Commissioner, supra*. As the Supreme Court has only recently held, in *United States v. National Association of Real Estate Boards*, decided May 8, 1950.

It is not enough that we might give the facts another construction, resolve the ambiguities differently, and find a more sinister cast to actions

which the District Court apparently deemed innocent. See *United States v. Yellow Cab Co.*, 338 U. S. 338, 342; *United States v. Gypsum Co.*, 333 U. S. 364, 394-395. We are not given those choices, because our mandate is not to set aside findings of fact "unless clearly erroneous".

Analysis of the record as a whole discloses that the Tax Court was entitled to afford weight to the following considerations which, among others, amply support its conclusion that Alaska Junk paid in the advances as contributions to capital, not as a loan:

1. The Tax Court clearly was warranted in regarding as far from conclusive the mere naming, by witnesses in oral testimony, the large advances in question made by the stockholders to Oregon Steel as "debts". Thus, even in the case of formal legal instruments in writing, it has repeatedly been held that (*In re Fechheimer Fishel Co.*, 212 Fed. 357, 360 (C. A. 2d), certiorari denied, *sub nom. Dellevie v. Fechheimer-Fishel Co.*, 234 U. S. 760)—

the fact that an instrument is called a "bond" is not conclusive as to its character. It is necessary to disregard nomenclature and look to the substance of the thing itself.

The misuse of words of art cannot change the legal conclusions. *Bakers' Mutual Coop. Ass'n v. Commissioner*, 117 F. 2d 27, 28 (C. A. 3d); *Hazel Atlas Glass Co. v. Van Dyk & Reeves*, 8 F. 2d 716, 720 (C. A. 2d), certiorari denied, *sub nom. Van Dyk v. Young*, 269 U. S. 570; *Commissioner v. Schmoll Fils Associated*, 110 F. 2d 611, 613 (C. A. 2d); *Brown-Rogers-Dirson Co. v. Commissioner*, *supra*, p. 349.

2. Again, on analogous reasoning the circumstance that the advances entered on "open account" (R. 42) in the books of Alaska Junk and of Oregon Steel were,



as taxpayer claims (Br. 9), classified on those books as "accounts receivable" and "accounts payable", respectively, the fact finder might regard on this record as of little consequence. These accounts were simply employed as convenient places in which to record all advances by Alaska Junk to Oregon Steel, no matter what their character namely, cash, merchandise, or merchandise procured for Oregon Steel, and were without distinction debited or credited, as the case might be, with stock subscriptions, debentures issued or payments. (R. 42, 65-66). They constituted a general catch-all for transactions of many kinds between the two businesses and the name given to the accounts in the books, the fact finder properly might regard as not significant. Here again the Tax Court was entitled to look to the actual facts, not to characterizations or names. *Doyle v. Mitchell Bros. Co.*, 247 U. S. 179, 187; *Thomas v. Commissioner*, 2 T. C. 193, 196.

3. No interest was charged at any time upon the books of Alaska Junk or otherwise by reason of the advances now claimed to be debt and *despite the circumstance that Alaska Junk maintained its books on the accrual basis*. (R. 34.) No interest was ever paid by the corporation on any advances by the stockholders. No interest was ever demanded from or promised to be paid by the corporation on any of the advances, upon which the loss here involved was realized, except on the purely temporary notes which taxpayers caused the corporation to execute for the balance of the advances, on open account, as of November 26, 1943, as an incident of the sale of their interest, and which notes were compromised with the purchasers the same day without any payment of interest. (R. 50-51.) Certainly, if taxpayers at any time had regarded the advances in question as debt absolutely payable, interest would have been accrued and credited to the taxpayer partners on account



of the alleged loans. This contemporaneous course of action, inuring to taxpayers' disadvantage, with respect to the advances is certainly more persuasive as to the true intent of the parties than the bare characterization made five years later by the friendly witnesses at the hearing.

4. With the exception of the notes above referred to, executed by Oregon Steel on November 26, 1943, immediately prior to and on the same day as the sale by taxpayers and Morris Schnitzer of their stock to the new owners (a) no notes, certificates, or other evidence of debt in any form were ever given by Oregon Steel to taxpayers or to Morris Schnitzer in recognition of any of the advances of the stockholders upon which taxpayers' claim for a bad debt deduction is founded; (b) Oregon Steel did not at any time by appropriate resolution of its directors or stockholders or otherwise recognize as debts, promise to pay, or assume liability for any of the advances by its stockholders, except to the extent of \$249,000 in debentures issued as discussed, *infra*, none of which, however, is included in the alleged bad debt deduction in issue here; (c) none of the advances made by the stockholders, except those for which the various debentures were issued, were due and payable by the corporation currently or at any future date. All these circumstances also assuredly afford grounds supporting inferences by the fact finder contrary to taxpayers' contentions. *Cohen v. Commissioner, supra*.

5. The evidence adduced by taxpayers and the record as a whole does not satisfy a strict rule of construction. Congress intended and allowed, as is well settled by the authorities cited, *supra*, strictly bad "debts" to be deducted under Section 23 (k) (1) of the Code and nothing else. The administration of a great revenue system is an intensely practical matter; Congress did not pur-

pose to grant deduction to ambiguous advances of the character here involved, subject to treatment at the taxpayers' option as debt or investment. To expand the meaning of the term "debts" to include the advances involved in the instant case, as the Supreme Court said, in *Equitable Society v. Commissioner*, 321 U. S. 560-564, "would indeed relax the strict rule of construction which has obtained in case of deductions under the various Revenue Acts."

A chronological analysis of the undisputed acts and dealings of taxpayers from the organization of Oregon Steel in June, 1941 (R. 40), until they sold their interest to the new owners on November 26, 1943 (R. 50-52), demonstrates that during this entire period of approximately two and a half years, there is not to be found any clear, unambiguous and binding expression by the stockholders, that the balance on the open account of Alaska Junk was intended by them to be debt. Tax-wise, a significant aspect of this course of dealing lies in the circumstance that if the operations of Oregon Steel had been successful, taxpayers, on the basis of their record actions prior to the date of sale (November 26, 1943) might far more convincingly have denoted the ambiguous open advances as capital investments. From this it would follow that in the hypothetical successful event of their venture, taxpayers would have been in a position to claim a higher basis for their stock, i.e., by treating as investment, the advances they now urge are loans. This would, of course, under many eventualities have then inured to their advantage tax-wise. It is submitted that the settled strict construction of the deduction provision, upon which taxpayers base their claim, required the trier of the facts to hold against taxpayers' contention in view of the ambiguity of taxpayers' undisputed dealings in the premises. In granting the bad debt or other deductions through exer-

cise of its legislative grace, Congress surely did not intend to permit a taxpayer vis-a-vis the Treasury to assume a position of "Heads I win, tails you lose". This consideration surely constitutes one of the important grounds for the settled rule of strict construction in deduction claims.

The following chronological statement of record facts demonstrates graphically the ambiguity of taxpayers' dealings with respect to these advances as well as further ample grounds for the Tax Court's conclusion:

*June 4, 1941.* Oregon Steel was organized and subscription to shares in the amount of \$187,800 made. (R. 40.)

*June 12, 1941.* No stock was actually issued except one formal qualifying share to each of the five subscribers. (R. 41.)

*June, 1941.* Morris Schnitzer attempted in vain to procure outside capital from New York investment houses. (R. 43.)

*October, 1941.* Alaska Junk commenced to make numerous advances to Oregon Steel, supplying it with goods of various kinds and paid bills for it. The amounts of cash advanced, bills paid, and value of goods furnished were charged by Oregon Steel to its open account with Alaska Junk. (R. 42.) Similarly, Morris Schnitzer advanced cash, paid bills and supplied goods, and these amounts, together with the expenses of his business trips, were charged to the corporation's account on his books (Schnitzer Steel Products Company). (R. 42.)

These advances were made as funds were needed by Oregon Steel and were available or procurable by the stockholders, and they continued for approximately two and a half years until sale of the shares to outside parties. No advance, whether by cash payment,



materials supplied or discharge of the corporation's bills and obligations, was specifically designated as made in satisfaction of a stock subscription, in payment for bonds, or as a loan. Throughout the whole period the advances were simply charged to open accounts receivable on the books of Morris Schnitzer and Alaska Junk and credited to open accounts payable on the corporation's books, and except for formal qualifying shares, no stock was issued until February 10, 1942, and no record of payment for that was made until March 31, 1943. (R. 67.) Substantially all the advances, with the exception of \$9,460 in iron scrap furnished with which to begin operations, were invested in the corporation's plant and equipment, namely, permanent assets. (R. 42, 65.)

*October, 1941.* Oregon Steel through its president, Morris Schnitzer, filed application with the Reconstruction Finance Corporation for a loan of \$600,000. He estimated that the plant would cost \$890,000, stating that capital was then \$187,700, but added (R. 43-44):

We expect to increase the capital of this corporation shortly. Additional stock will be taken by S. Schnitzer and J. Wolf to equal that of M. Schnitzer.

*October, 1941.* When taxpayers as partners in Alaska Junk began to charge advances to the corporation's open account, they had every reason to believe that the authorized capital of \$250,000, and the subscribed capital of \$187,800, were only a fraction of the minimum capital needed for the construction of a steel mill, which eventually cost \$1,400,000. (R. 43, 49, 64-65.)

*November, 1941.* Bank of America refused loan because the authorized capital was deemed too small. (R. 43.)

*February, 10, 1942.* Stock for the first time actually issued. (R. 41, 67.)

*April, 1942.* The Bank of Portland refused loan despite oral assurances by the corporation's officers that \$1,000,000 would be invested in the plant and more would be available for working capital. (R. 43.)

*April 2, 1942.* The executive committee of the Reconstruction Finance Corporation approved loan, subject to listed conditions. (R. 44.)

*November, 1942.* Actual construction of the mill began. (R. 42.)

*November 30, 1942.* Oregon Steel account with Alaska Junk showed a debit balance of \$299,069.70, and its account with Schnitzer Steel Products Company, a debit balance of \$138,984.11. Thus, at that time the open account for these advances was greatly in excess of the par value of issued stock (\$187,800). (R. 42-43, 65.)

In a writing Morris Schnitzer referred to these advances as "contributed capital" (Resp. Ex. Q, admitted R. 157-159), printed in full in the footnote.<sup>6</sup>

6

#### OREGON ELECTRIC STEEL ROLLING MILLS

##### Certificate of Contributions of Capital

I, Morris Schnitzer, President of Oregon Electric Steel Rolling Mills, hereby certify that as of November 30, 1942, Alaska Junk Company, a partnership composed of Sam Schnitzer, Rose Schnitzer, H. J. Wolf and Jennie Wolf, had contributed capital to Oregon Electric Steel Rolling Mills in the sum of \$299,069.70; that as of the same date I personally had contributed capital to said Oregon Electric Steel Rolling Mills in the sum of \$138,984.11; that said last named amount was contributed by me under the name of Schnitzer Steel Products Company which is a registered assumed name used by me; that there will be issued to such contributors, including myself, common stock in said corporation at par in the sum of \$187,700.00 and the balance in the debentures of said corporation in the form heretofore submitted to Reconstruction Finance Corporation containing a standby as to principal and interest until after the payment in full of the mortgage loan from Reconstruction Finance Corporation to said Oregon Electric Steel Rolling Mills, which debentures will be taken at par; that the authorized capital stock of said corporation is \$250,000.00, and for advances made subsequent to Novem-



By inadvertence the Tax Court apparently attributed this document to Sam Schnitzer instead of to his son Morris. (R. 43.) Taxpayers' attempt to make much (Br. 9, 19) of this minor discrepancy in the Tax Court's careful and detailed findings with respect to the numerous and complex transactions between the parties, although conceding (Br. 19) "THE PRIMARY FACTS FOUND ARE CORRECT IN THE MAIN."

In any event, this inadvertence is completely harmless to taxpayers, for in Respondent's Exhibit R, quoted and discussed immediately, *infra*, Sam Schnitzer did refer there to identical advances by Alaska Junk in the sum of \$299,069.70 as "contributed as a capital investment". Exhibits Q and R are obviously contemporaneous; Exhibit R is seemingly the rewritten form of Exhibit Q, and was "put in the file". The Tax Court referred to it as "an office memorandum". (R. 43.) Under the circumstances taxpayers' contention (Br. 19) that the Tax Court "seriously erred" in attributing the statement contained in Exhibit Q to Sam Schnitzer, that this inadvertence, especially in view of Sam Schnitzer's signature to Exhibit R, constituted "prejudice" and, indeed, in their asserted inability to identify the Tax Court's reference (R. 43), must be regarded as more ingenious than serious.

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ber 30, 1942 there will be issued either stock at par within the amount authorized or debenture in said form at par.

(signed) MORRIS SCHNITZER,

*President,*

*Oregon Electric Steel Rolling Mills.*

[In handwriting]:

I hereby agree as owner of Schnitzer Steel Products will accept stock or debentures in amounts of my claim of approximately \$138,984.11 in full settlement of my claim against the OESRM, for materials and equipment furnished them.

MORRIS SCHNITZER.

[In handwriting]:

Mark—Altho rewritten, this may be put in the file for whatever it is worth.

REC.

*December 1, 1942.* Taxpayers Sam Schnitzer and Wolf as partners of Alaska Junk wrote Reconstruction Finance Corporation that the cost of the mill might exceed \$1,200,000, and that Alaska Junk would furnish any necessary money in excess thereof to complete the project, if Reconstruction Finance Corporation would lend an additional \$100,000. (R. 44, Resp. Ex. U.)

*December 4, 1942.* Reconstruction Finance Corporation approved loan of \$700,000. Oregon Steel gave its note secured by a mortgage for that amount, payable within five years by monthly instalments of \$6,500 from May 1, 1943, and by additional annual payments sufficient to make all payments equal to 50% of the corporation's net earnings for the preceding year. The note was secured by a mortgage. (R. 44-45.)

*December, 1942.* Morris, Sam and Rose Schnitzer, and Harry J. and Jennie Wolf individually guaranteed repayment of the note, and bound themselves to supply "additional working capital" in amounts deemed satisfactory by Reconstruction Finance Corporation as long as any part of the loan should remain unpaid. (R. 45.)

*December, 1942.* The corporation Oregon Steel bound itself to limit officers' annual salaries, as long as any part of the Reconstruction Finance Corporation loan should remain unpaid, to a total of \$25,000, and to pay in cash no more than \$15,000. (R. 45.)

*December 29, 1942.*<sup>7</sup> In an instrument entitled "Agreement Regarding Capital Investment" Oregon Steel by Morris Schnitzer as president, Morris Schnitzer as sole owner of Schnitzer Steel Products Company, and Alaska Junk Company, by Sam Schnitzer, as a general partner, represented and agreed with Recon-

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<sup>7</sup> In the findings the date of the instrument is inadvertently stated as December 29, 1941.

struction Finance Corporation (R. 45-46, Resp. Ex. R, admitted R. 159) :

Alaska Junk Company has contributed as a capital investment in Borrower the sum of \$299,069.70, such investment being in the form of cash or of property at its true and reasonable value.

Morris Schnitzer has contributed a capital investment in Borrower in the sum of \$138,984.11, such investment being in the form of cash or of property at its true and reasonable value.

Such contributions by Stockholders have, as stated, been as a capital investment, and in no wise as outstanding accounts payable by Borrower, except to the extent that Borrower's debenture notes may be issued for a part of such contributions or capital investment.

Stockholders covenant that they will receive, in full payment of all such capital investments so made by them respectively, only the common stock of Borrower, or debenture notes of Borrower (on the form heretofore submitted to and approved by RFC, which form expressly provides that no payment of principal or interest thereon may be made prior to the repayment in full of the loan from RFC to Borrower evidenced by the latter's note for \$700,000.00 dated December 15, 1942); and Borrower covenants to evidence such capital investments in no other way, or to repay any of such investments in any manner other than in the form of said debenture notes.

After its loan was made the Reconstruction Finance Corporation did allow reimbursements of subsequent advances to the amount of \$114,519 (R. 46, 61), but the Tax Court was certainly not clearly wrong in inferring that the release of these corporate funds was a special favor designed to aid Alaska Junk which was then in financial straits, so that it could make advances for essential equipment of materials needed in mill construction. Thus, the Reconstruction Finance Corpo-

ration did no more than release a part of the \$700,000 loan for a specific purchase for the steel mill through Alaska Junk, and in order to obtain materials needed in the mill construction. (R. 70.)

*January 12, 1943.* While the final terms of the Reconstruction Finance Corporation loan were being arranged, Wolf expressed dissatisfaction because Morris Schnitzer, holding two-thirds of the corporate stock, had not made a proportionate part of the advances. Cost of the enterprise had already exceeded anticipation (R. 46) and Morris was financially unable to advance more. Pursuant to an oral agreement, Morris Schnitzer promised taxpayers that he would bear one-third of any loss that might result from the total amounts advanced by the partners of Alaska Junk and himself to the corporation, over and above the advances credited to stock subscriptions. Alaska Junk, in turn, agreed to bear two-thirds of any such loss. Morris Schnitzer and Alaska Junk continued thereafter to make advances as before and these advances were credited to their open accounts with the corporation in the same way as before and charged to the corporation's open account with them. (R. 48.)

Debenture bonds in the amount of \$249,000 were issued to the stockholders on terms contemplated by the understanding with Reconstruction Finance Corporation. (R. 46-47.) Of these bonds, the partners of Alaska Junk received a total of \$174,000. The bonds bore 8% interest and were payable within ten years of issue, and no payment of interest or principal could be made while any balance remained due on the corporation's \$700,000 note to Reconstruction Finance Corporation. (R. 46-47.)

*March 11, 1943.* As further part of the settlement agreement with Morris Schnitzer, he surrendered ap-



proximately half of his shares of stock, and these were reissued to the partners of Alaska Junk so that the corporation's outstanding 1,878 shares were thereafter held approximately two-thirds by the partners of Alaska Junk and one-third by Morris Schnitzer. (R. 47, 67.)

*March 31, 1943. For the first time entries were made on the books of Oregon Steel of payment for the corporate shares.* These entries were made in the open account with Alaska Junk and were for the shares, not as originally issued but as redistributed. At the same time credits were made in the open account regarding payment for the debentures, namely, in the amount of \$174,000 on account of the debentures, and \$124,900 in payment for stock at its par value. Nevertheless, after these credits were taken, there still remained over \$315,000 in the open account, which is reflected in the ultimate balance that taxpayers now seek to characterize as a loan. (R. 47-48, Pet. Ex. 17, p. 4, Account of Alaska Junk, General Ledger, Oregon Steel.) It is significant as throwing further doubt upon taxpayers' claim, that on Alaska Junk's own books corresponding entries of this neat sum aggregating \$298,200 for payment of stock and debentures were not made until July 14, 1943. (R. 47-48, Pet. Ex. 26, p. 64, General Account of Oregon Steel on books of Alaska Junk.)

The Tax Court was warranted in inferring from this delay (R. 68)—

we can not but share the bookkeeper's probable feeling that the entries made little difference anyhow because the advances were all of the same character and could be distributed as desired among accounts for capital contributed, bonds issued and loans payable.



*March 18, 1943.* Morris Schnitzer wrote Reconstruction Finance Corporation that costs were rising and that (R. 48)—

the stockholders had “in this job over \$700,000 of our own money,” but “never originally intended to put in over \* \* \* the \$500,000 we were supposed to put in as our share in the capital investment.”

*March 31, 1943.* Even after the March, 1943, settlement, Alaska Junk continued to make large advances to Oregon Steel so that by November 26, 1943, their total from the beginning aggregated over \$800,000 (R. 50-51, 65), and substantially all, with the possible exception of \$9,460 in iron scrap, had apparently been invested in the corporation's organization and plant, as a permanent asset (R. 65).

*June, 1943.* Mill finally completed at a cost of \$1,400,000, and the melting of scrap into ingot started. (R. 49.)

*June, 1943.* Morris Schnitzer entered military service. (R. 49.)

*June, 1943.* Oregon Steel began to borrow relatively small loans from banks. (R. 49.)

*July 14, 1943.* As above noted, entries first made in Alaska Junk's books on its open account of credits reflecting payment for stock and debentures, which had been made in Oregon Steel's books on March 31, 1943. (R. 47-48.)

*November, 1943.* Small loans from banks secured by steel inventory and warehouse receipts for scrap, aggregated approximately \$150,000. (R. 49.)

*November, 1943.* Operations of mill unsuccessful and stockholders decided to cease operations and to dispose of property. (R. 49-50.)

*November 26, 1943.* Stockholders sold all their shares to Hall and Mears for nominal amount of one cent

a share. Before so doing, and on the same day, they had the corporation give to Schnitzer Steel Products (Morris Schnitzer) its promissory note for \$26,829.28, and to Alaska Junk its promissory note for \$427,843.87, which were equal to the respective credit balances shown on that date in the payees' open accounts with the corporation. (R. 50-51.) As part of the price of the sale, Alaska Junk received from the purchasers new 6% notes of Oregon Steel in the amount of \$174,000, being the face amount of the debentures already issued, and in addition, \$142,200.33 in new notes of the purchasers in exchange for the former debentures and the newly made notes of the same day. (R. 51, 61.)

*November 26, 1943.* The entry of this date in the open account on Alaska Junk's books (R. 51-52, 69, Pet. Ex. 26), being the last entry preceding transfer of the account to "Bad Accounts", computed the amount due from Morris Schnitzer, by reason of his agreement to bear one-third of the loss, and computed the loss on the basis of the total advances of Morris and Alaska Junk from the beginning, not merely on the basis of the amounts in open account remaining after credits for stock subscriptions and bonds (R. 391-397; Pet. Ex. 66). Thus, the total loss was regarded by taxpayers as including all advances, whether contributed to stock, bonds, or loans, and *in proportion to stockholdings*. This, the Tax Court was entitled to deem "a considered expression of the parties' own view". (R. 69.)

In summary then, from these record facts the Tax Court was entitled to infer that all along no clear intent existed to treat the advances here involved as debt and that not until the very day of the sale to outside parties, November 26, 1943, was it decided to designate them as debt, which was done by way of the purely temporary expedient of a note cancelled the same day.

Thus, there is certainly present here (*John Kelley Co. v. Commissioner, supra*, p. 525)—

the wholly useless temporary compliance with statutory literalness which this Court condemned as futile, as a matter of law, in *Gregory v. Helvering*, 293 U. S. 465.

No evidence of indebtedness was issued until the moment of the alleged debt loss. Since taxpayers conducted their transactions thus enigmatically, they cannot complain if, especially where a claim of deduction is involved, the fact finder construed them to constitute what they were in substance, i.e., investments in permanent capital assets. At the time the debentures were issued in March, 1943, and payment for the stock credited against the open account, as has been seen, over \$300,000 still remained in the open account, which is reflected in the ultimate balance that taxpayers now seek to characterize as a loan. (R. 47, 68.) The Tax Court was entitled to infer that had taxpayers actually regarded this open balance as debt and not capital investment, it would have been so allocated at the time the debentures were issued. Instead, for a period of approximately eight months thereafter during which Alaska Junk continued to make large advances (R. 65), no such allocation was made. Moreover, for a substantial period after March 31st, the stockholders obviously retained optimism of eventual success. The mill started operation in the following June, 1943, and it was not until then that Morris Schnitzer entered military service. (R. 49.) Operations continued, as has been seen, through October, 1943, and taxpayers may well have regarded it as to their advantage to treat the balance in open account as investment during all of this time. The Tax Court might infer that not until it was concluded that the venture was a failure, was an

effort made definitely to designate this balance as loans. Congress intended to allow the bad debt deduction only in clear cases of debt; otherwise, contrary to the public interest, a taxpayer may play fast and loose with his tax obligation.

Moreover, during the entire period under consideration, accepted indicia of debt were absent, such as fixed maturity date for payment, agreement on interest rate, accrual of interest, no subordination to creditors, divorce from management, security, written evidence of indebtedness, timely and clear entry in purported creditor's books. Under these circumstances the extensive priority granted to the Reconstruction Finance Corporation loan, under which the corporation could not make payments on any account to stockholders, except \$15,000 annually as salaries, the Reconstruction Finance Corporation mortgage, the pledging of inventory and like assets, not covered by the Reconstruction Finance Corporation mortgage, to secure bank loans (R. 68), and the execution of debentures as to part of the advances, in the aggregate, constitute practically an admission that the balance of the advances were intended to be risk capital; certainly this interpretation holds taxwise in strict construction of a deduction from gross income.

As a matter of fact, there is no ambiguity in taxpayers' transactions. The numerous contemporary statements and acts of the parties inconsistent with claim of debt, set forth in detail above and in the Tax Court's findings (R. 43-46, 48-49, 67-69), nullify the conclusory testimony of intent to loan offered at the hearing. Certainly, on this record the trier of the facts, weighing the evidence, might properly so find.

Taxpayers and Morris Schnitzer completely managed and controlled as well as owned their alleged debtor. (R. 41-42.) As this Court held in *Wilshire*



*West. Sandwiches v. Commissioner*, 175 F. 2d 718, 21:

The effect of a lending and investing transaction giving creditors, as stockholders, proprietary interest in proportion to their loans, subjects the transaction to close scrutiny,

even though, as a matter of law, the transaction need not be regarded as a stock investment, regardless of intent. The proportional financial interest of taxpayers in Oregon Steel was exactly the same, whether created as stockholders or creditors, as appears from the stockholders' agreement, the closing entry on the Alaska Junk books (R. 69) and the testimony of Morris Schnitzer (R. 127-128). The Tax Court might properly regard, as it did, the mere existence of such an agreement incompatible with testimony that repayment of advances was anticipated or with their characterization as loans and, further, that such a situation is an incident of stock ownership, not of a debtor-creditor relation. (R. 69.) Thus, subjecting the instant transaction to "close scrutiny", the Tax Court was warranted in concluding from all the circumstances that no debt transaction was involved.

6. Another factor whereby the Tax Court was warranted and did test the reality of the claim by these stockholders of a debtor-creditor relationship is strikingly present in this record, namely the ratio of debt, in the face of their claim, to investment. (R. 66.) Especially in view of the ambiguity and inconsistency of taxpayers' transactions with Oregon Steel, this criterion derives significance here. The instant situation is that of "an obviously excessive debt structure", adverted to by the Supreme Court in *John Kelley Co. v. Commissioner*, *supra*, as follows (p. 526):

As material amounts of capital were invested in stock, we need not consider the effect of extreme



situations such as nominal stock investments and an obviously excessive debt structure.

Thus under taxpayers' claim here, the capital invested in stock amounted to \$187,800 as against a debt structure of more than \$1,500,000. (Balance Sheet, Oregon Steel, October 31, 1943, Pet. Ex. 19.) Again, as against an asserted investment of only \$187,800, according to taxpayers' claim, the corporation owed to its stockholders a total of more than \$700,000. With respect to a similar situation the Court of Appeals for the Fifth Circuit in *Arnold v. Phillips*, 117 F. 2d 497, certiorari denied, 313 U. S. 583, held as follows (p. 501):

Those [advances] made before the enterprise was launched were, as the district court found, really capital. Although the charter provided for no more capital than \$50,000, what it took to build the plant and equip it was a permanent investment, in its nature capital. There was no security asked or given. Arnold saw that he could not proceed with his enterprise unless he enlarged the capital. There can be little doubt that what he contributed to the plant was actually intended to be capital, notwithstanding the charter was not amended and demand notes were taken. The district court was justified in concluding as a matter of fact that the advances during the first year were capital, a sort of interest-bearing redeemable stock; and that as a matter of law these contributions could not, as against corporate creditors, either precedent or subsequent, be turned into secured debts by afterwards taking and recording a trust deed to secure them. *There was no debt to be secured.* (Italics supplied.)

While the cited case arose in a bankruptcy situation, it is notable that the holding of the court is placed upon the broad ground, irrelevant to bankruptcy, that "There was no debt to be secured". Here also

substantially all the stockholders' advances were invested in original plant and equipment, namely, permanent capital investment.

Again, in a case where the attributes of legal form were far more fully complied with than in the instant record, the Tax Court in *1432 Broadway Corp. v. Commissioner*, 4 T.C. 1158, 1164-1165, said:

The debentures are in approved legal form, and, if their legal attributes alone were determinative of the character of the interest accruals, there would be little room for doubt that they were the indebtedness they purport to be. Cf. *Clyde Bacon, Inc.*, 4 T. C. 1107. But, for tax purposes, their conformity to legal forms is not conclusive. Although a taxpayer has the right to cast his transactions in such form as he chooses, and the form he chooses will generally be respected, the Government is not required to acquiesce in the taxpayer's election of form as necessarily indicating the character of the transaction upon which his tax is to be determined. "The Government may look at actualities and upon determination that the form employed for doing business or carrying out the challenged tax event is unreal or a sham may sustain or disregard the effect of the fiction as best serves the purposes of the tax statute." *Higgins v. Smith*, 308 U. S. 473. See also *Commissioner v. Court Holding Co.*, 324 U. S. 331. The Government is not bound to recognize as the substance or character of a transaction a technically elegant arrangement which a lawyer's ingenuity has devised. *Griffiths v. Commissioner*, 308 U. S. 355.

The cited case was affirmed by the Court of Appeals for the Second Circuit in 160 F. 2d 885, where it was pointed out that the Tax Court had "denied deduction on the ground that the evidence did not show that the debentures were, or were intended to be, evidences of indebtedness"; they were 'more nearly like

preferred stock than indebtedness'." While the Court of Appeals, in view of the *John Kelley* case, *supra*, regarded these conclusions as not within the scope of its judicial review, it further stated:

We may add, however, that, if the question were open to us, we should reach the same result as did the Tax Court.

See also to the same effect *Thomas v. Commissioner*, 2 T. C. 193; *Janeway v. Commissioner*, 2 T. C. 197, affirmed, 147 F. 2d 602 (C.A. 2d); *Swoby Corp. v. Commissioner*, 9 T. C. 887; Semel, Tax Consequences of Inadequate Capitalization, 48 Columbia L. Rev. 202 (March, 1948).

Again, the Tax Court was warranted in considering the testimony at the hearing to the effect that the ratio of investment to debt in a soundly financed similar enterprise is expected to be two to one, or at the least one to one. The owners of the business should have as much or more in it than the creditors. (R. 430-433, 504-505, 519.)

On the other hand, the Tax Court was warranted in finding unpersuasive, the taxpayers' claim that they reasonably anticipated such large operation profits from the new venture as to pay off this overwhelming debt structure. This claim is refuted, for example, by the acceptance of debentures in the amount of \$249,000 absolutely due only in ten years and subject to the R.F.C. mortgage of \$700,000. The circumstances that in the hands of experienced owners and, due inferentially to the requirements of the war, Oregon Steel did earn large profits for the new owners, could not require in view of all the circumstances, the Tax Court, as a matter of law, to be persuaded by taxpayers' contention with respect to repayment. (R. 66.)

*C. The Tax Court correctly applied the relevant authorities*

As already discussed in subpoint A, *supra*, the issue here is one of fact. Hence, since each case is necessarily confined to its peculiar facts, the numerous authorities, some of which have already been cited, dealing with similar questions,<sup>8</sup> namely, whether an advance by a stockholder is to be regarded as a loan or as a capital contribution, for purposes of asserted bad debt or interest deductions are helpful principally as guides. Indeed, in many instances, it is impossible to select single factors which can be pointed to as decisive, for elements both of obligation and of stock are commonly embodied in the evidence. The primary facts may be undisputed, as substantially they are here, but conflicting inferences may reasonably be drawn from them, and it is the peculiar and primary province of the fact finder to draw these and weigh the evidence in the light of these inferences. This is the lesson of the *John Kelley* case, *supra*, where the Supreme Court declared (p. 530):

The Tax Court is fitted to decide whether the annual payments under these corporate obligations are to be classified as interest or dividends. The Tax Court decisions merely declare that the

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<sup>8</sup> See, e.g., *Wilshire & West. Sandwiches v. Commissioner*, *supra*; *Maloney v. Estate of Spencer*, 172 F. 2d 638 (C. A. 9th); *1432 Broadway Corp. v. Commissioner*, 4 T. C. 1158, affirmed, 160 F. 2d 885 (C. A. 2d); *Cohen v. Commissioner*, *supra*; *Janeway v. Commissioner*, 2 T. C. 197, affirmed, 147 F. 2d 602 (C. A. 2d); *Van Clief v. Helvering*, 135 F. 2d 254 (C. A. D.C.); *Commissioner v. Meridian & Thirteenth R. Co.*, 132 F. 2d 182 (C. A. 7th); *Pacific Southwest Realty Co. v. Commissioner*, 128 F. 2d 815 (C. A. 9th), certiorari denied, 317 U. S. 663; *Commissioner v. Schmoll Fils Associated*, 110 F. 2d 611 (C. A. 2d); *United States v. South Georgia Ry. Co.*, 107 F. 2d 3 (C. A. 5th); *Commissioner v. Proctor Shop*, 82 F. 2d 792 (C. A. 9th); *Commissioner v. O.P.P. Holding Corp.*, 76 F. 2d 11 (C. A. 2d).



undisputed facts do or do not bring the payments under the definition of interest or dividends. The documents under consideration embody elements of obligations and elements of stock. There is no one characteristic, not even exclusion from management, which can be said to be decisive in the determination of whether the obligations are risk investments in the corporation or debts.

While, subsequent to the decision in the *John Kelley* case, the scope of review over factual decisions of the Tax Court has, of course, been extended, through the legislative repeal of *Dobson v. Commissioner*, 320 U. S. 489, rehearing denied, 321 U. S. 231, by amendment to Section 1141 (a) of the Internal Revenue Code (see fn. 4, *supra*), the essential factual nature of the problem remains the same,<sup>9</sup> and in this important respect, among others, the rule laid down by the Supreme Court in the *Kelley* case remains the law. Thus, although, since the demise of *Dobson*, the appellate courts are not limited in review of Tax Court decisions to clear cut questions of law, nevertheless, the Tax Court or the District Court remain the fact finders, and as the Supreme Court recently pointed out in *United States v. National Association of Real Estate Boards*, *supra*, it is not enough that an appellate court might give the facts another construction or resolve the ambiguities differently, the appellate scope of review is limited "because our mandate is not to set aside findings of fact 'unless clearly erroneous'." Applying these principles here, it is submitted that the factual conclusion reached by the fact finder in weighing the evi-

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<sup>9</sup> See, to the same effect, *Boehm v. Commissioner*, *supra*, p. 293, where the Supreme Court said:

The circumstance that the facts in a particular case may be stipulated or undisputed does not make this issue any less factual in nature. The Tax Court is entitled to draw whatever inferences and conclusions it deems reasonable from such facts.



lence and the inferences to be drawn from it, construing and resolving its ambiguities, was correct and certainly cannot be regarded on review as clearly erroneous.<sup>10</sup>

Similarly on these principles the decision below for many reasons cannot fairly be regarded in variance with the recent decisions of this Court in *Maloney v. Spencer, supra*, and *Wilshire & West. Sandwiches v.*

<sup>10</sup> Taxpayers also argue that the Tax Court failed to make findings with respect to advances made to a certain National Machinery Company and Hesse Ersted Company, supposed to be indicative of other transactions, and in the case of the first of which a bad debt deduction had been taken. (Br. 21-22.) It is asserted that consideration to these items was necessary in order for the Tax Court to give proper weight to the record. (Br. 22.) However, similar items were explicitly found by the Tax Court (R. 38-39), and it is certainly not necessary for the trier of the facts to advert to every detail of a long record in its findings nor reasonable to assume that aspects of the evidence were disregarded, merely because explicit mention is not made of them.

Taxpayers further criticize the statement in the findings (R. 42):

From October 1921 Alaska Junk made numerous advances of cash to Oregon Steel; supplied it with goods of various kinds at cost and paid bills for it. The amounts of cash advance, the bills paid and value of the goods furnished were charged to its open account with Alaska Junk

on the ground that the goods were not supplied "at cost" (Br. 9-21). The record contains evidence, however, that the goods were certainly sometimes supplied at cost. (R. 215-216.) Moreover, it is obvious that there is no parallel between the advances of merchandise here intended to form part of the permanent structure of Oregon Steel and advances of merchandise by a manufacturing parent corporation to a sales subsidiary for general distribution to the public. In any event, any inaccuracy in completeness of the statement criticized was harmless and does not indicate that the Tax Court misunderstood the situation in prejudice to the result, for, as the Tax Court subsequently noted (R. 670):

No advance, whether by cash payment, materials supplied or discharge of the corporation's bills and obligations, was specifically designated as made in satisfaction of a stock subscription, in payment for bonds, or as a loan.

The primary facts found by the Tax Court, covering the mass of evidence and exhibits introduced and a complex factual situation were concededly "correct in the main". (Br. 19.)

*Commissioner, supra*, as apparently taxpayers contend. (Br. 11, 46-48.) This case depends on its facts and those on theirs. Moreover, in the *Spencer* case, the factual conclusion of the District Court was affirmed. In addition there, for instance, this Court emphasized the consistent treatment both in actions and bookkeeping of the parties throughout the taxable years in regard to the advances (p. 641), evidencing the debtor-creditor relation, as well as notes given by the taxpayers to the corporations, absent in the instant case. Here, as particularized above, there was substantial evidence in books, transactions and writings, inconsistent with the claim of debt.

Again, in *Wilshire & West. Sandwiches, supra*, while this Court reversed the Tax Court finding and sustained an interest deduction, the facts there are in striking contrast with those here. Promissory notes maturing in two years at 6% interest, payable quarterly, were issued there for the asserted loans, and though not paid in time, were paid in full, both as to interest and principal. Further, this Court placed special emphasis upon the finding of the Tax Court there that the parties originally actually intended to loan the money. Indeed, this Court's disagreement with the Tax Court in the cited case seems essentially limited to the latter's inference from other facts and circumstances that the original intent to loan was subsequently nullified.

Thus, the cited case has little bearing here, where, for example, no notes were ever given, except the merely formal and temporary ones made on the day they were cancelled, November 26, 1943, and substantially as part of the sale of the stockholders' interest in Oregon Steel to outside parties. Here no interest was charged, demanded, accrued or paid. Again, here the Tax Court made no finding of intent to loan at any time. Surely, subjecting here the asserted lending and investing

transaction, giving creditors, as stockholders, proprietary interest in proportion to their alleged loss, to the "close scrutiny" which this Court in the cited case (p. 721) declared proper, the Tax Court's conclusion on the instant record of no debt is completely compatible with the decision of this Court in the cited case. While here, also, as there, there may be features looking both ways, it surely was not clear error for the Tax Court to conclude on this very different record from that involved in *Wilshire & West. Sandwiches*, that the features sustaining an investment transaction here predominated.

Certainly, the decision of the instant issue is not determined solely by the parties conclusory characterizations of their intent and the Tax Court did not err in weighing the evidence in the light of all of the indicia (R. 63-64) above referred to and repeatedly recognized and applied in *John Kelley Co. v. Commissioner, supra*, and other authorities above cited. (Fn. 8.)

## II

### **In Any Event, the Loss Did Not Occur in Taxpayers' Trade or Business and the Amount of the Deduction Is under Section 23 (k) (4) of the Code Limited to Capital Loss Rates**

Furthermore, should this Court hold, contrary to our contention in Point I, *supra*, that debts did result from the advances, nevertheless they were not business debts and, hence, as provided by Section 23 (k) (4) of the Code (Appendix, *infra*), are considered as a loss from the sale or exchange of a capital asset held for not more than six months and deductible only at the capital loss rates. (Sec. 117.) The Tax Court, in view of its decision in favor of the Commissioner that the advances did not result in a bad debt, found it unnecessary to consider this contention with respect to the business character of the alleged loan (R. 70), also made



by the Commissioner below (R. 62). However, the Tax Court did make fact findings with respect to loans or advances occasionally made to customers by Alaska Junk in the expectation of maintaining or increasing its trade, and also that Alaska Junk made very large advances to enterprises in which members of the Wolf and Schnitzer family were interested. (R. 38-40.)

Section 23 (k)(4) defines a "non-business debt" as "other than a debt the loss from the worthlessness of which is incurred in the taxpayer's trade or business." The pertinent Treasury Regulations (Regulations 111, Sec. 29.23 (k)-6, Appendix, *infra*), provides:

The question whether a debt is one the loss from the worthlessness of which is incurred in the taxpayer's trade or business is a question of fact in each particular case. The determination of this question is substantially the same as that which is made for the purpose of ascertaining whether a loss from the type of transaction covered by section 23 (e) is "incurred in trade or business" under paragraph (1) of that section.

The character of the debt for this purpose is not controlled by the circumstances attending its creation or its subsequent acquisition by the taxpayer or by the use to which the borrowed funds are put by the recipient, but is to be determined rather by the relation which the loss resulting from the debt's becoming worthless bears to the trade or business of the taxpayer. If that relation is a proximate one in the conduct of the trade or business in which the taxpayer is engaged at the time the debt becomes worthless, the debt is not a non-business debt for the purposes of this section.

Applying this standard, quoted from the pertinent Regulations, that—

the relation which the loss resulting from the debt's becoming worthless bears to the trade or business of the taxpayer

the findings (R. 38-40) merely show that taxpayers went into various lines of business together, which they as entrepreneurs necessarily financed themselves. There is no evidence that they financed any other business enterprises as such in which they had no financial interest. True, they made advances to haulers and contractors in the nature of prepayments for hauling or procuring iron and steel scrap for them, but this is a far cry from the financing business. The Tax Court found that Alaska Junk was (R. 33-34)—

engaged in the business of buying, selling and generally dealing in junk, pipe, tools, machinery, hardware, scrap and other metal products in Portland as, indeed, it is in substance stipulated (R. 529).

Certainly it is not a normal incident of the business of selling iron and steel scrap or of selling finished steel to go into the business of manufacturing steel as taxpayers did. To say so is to say that the tail can wag the dog. The factual situation here is readily differentiated from that in *Maloney v. Spencer, supra*.

Moreover, the situation here does not fall within any one of the six illustrations contained in the controlling Regulations (Appendix, *infra*), which clarified the meaning of the proximate relationship there defined; for every illustration reflects a debt resulting from a sale of goods in the ordinary course of business. Here, while part of the advances consisted of merchandise from the inventories of Alaska Junk, such advances did not involve sales in the regular course of business. Moreover, even if they did, there is no evidence to show that part, if any, of the remainder of the advances upon which the loss here claimed was sustained, consisted of these merchandise advances as distinguished from cash advances.

It is therefore respectfully submitted that the debts, if such they were, were non-business debts and that the



deduction for loss thereon must be limited in amount to capital loss rates in accordance with the mandate of the statute.

CONCLUSION

The decisions of the Tax Court are correct and should be affirmed.

Respectfully submitted,

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MAY, 1950.

## APPENDIX

## STATUTE AND REGULATIONS INVOLVED

## Internal Revenue Code:

## SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

\* \* \* \* \*

(k) [As amended by Section 124 (a) of the Revenue Act of 1942, c. 691, 56 Stat. 798, and Section 113 (a) of the Revenue Act of 1943, c. 63, 58 Stat. 21] **BAD DEBTS.**—

(1) *General Rule.*—Debts which become worthless within the taxable year; or (in the discretion of the Commissioner) a reasonable addition to a reserve for bad debts; and when satisfied that a debt is recoverable only in part, the Commissioner may allow such debt, in an amount not in excess of the part charged off within the taxable year, as a deduction. This paragraph shall not apply in the case of a taxpayer, other than a bank, as defined in section 104, with respect to a debt evidenced by a security as defined in paragraph (3) of this subsection. This paragraph shall not apply in the case of a taxpayer, other than a corporation, with respect to a non-business debt, as defined in paragraph (4) of this subsection.

\* \* \* \* \*

(4) *Non-Business Debts.*—In the case of a taxpayer, other than a corporation, if a non-business debt becomes worthless within the taxable year, the loss resulting therefrom shall be considered a loss from the sale or exchange, during the taxable year, of a capital asset held for not more than 6 months. The term "non-business debt" means a debt other than a debt evidenced by a security as defined in paragraph

(3) and other than a debt the loss from the worthlessness of which is incurred in the taxpayer's trade or business.

(26 U.S.C. 1946 ed., Sec. 23.)

Treasury Regulations 111, promulgated under the Internal Revenue Code:

SEC. 29.23 (k)-6 [As amended by T. D. 5458, 1945 Cum. Bull. 45]. **NON-BUSINESS BAD DEBTS.**—In the case of a taxpayer, other than a corporation, if a non-business bad debt becomes entirely worthless within a taxable year beginning after December 31, 1942, the loss resulting therefrom shall be treated as a loss from the sale or exchange of a capital asset held for not more than six months. Such a loss is subject to the limitations provided in section 117 with respect to gains and losses from the sale and exchange of capital assets. A loss with respect to such a debt will be treated as sustained only if and when the debt has become totally worthless, and no deduction shall be allowed for a non-business debt which is recoverable in part during the taxable year. Nor are the provisions of this subdivision applicable in the case of a loss resulting from a security as defined in section 23 (k)(3). A non-business debt is a debt other than a debt the loss from the worthlessness of which is incurred in the taxpayer's trade or business and other than a debt evidenced by a security as that term is defined in section 23 (k)(3). The question whether a debt is one the loss from the worthlessness of which is incurred in the taxpayer's trade or business is a question of fact in each particular case. The determination of this question is substantially the same as that which is made for the purpose of ascertaining whether a loss from the type of transaction covered by section 23 (e) is "incurred in trade or business" under paragraph (1) of that section.

The character of the debt for this purpose is not controlled by the circumstances attending its crea-

tion or its subsequent acquisition by the taxpayer or by the use to which the borrowed funds are put by the recipient, but is to be determined rather by the relation which the loss resulting from the debt's becoming worthless bears to the trade or business of the taxpayer. If that relation is a proximate one in the conduct of the trade or business in which the taxpayer is engaged at the time the debt becomes worthless, the debt is not a non-business debt for the purposes of this section.

To illustrate: A, an individual engaged in the grocery business and who makes his income tax returns on the calendar year basis, extends credit on an open account to B in 1941.

(1) In 1942 A sells the business but retains the claim against B. The claim becomes worthless in A's hands in 1943. A's loss is controlled by the non-business debt provisions. While the original consideration was advanced by A in his trade or business, the loss was not sustained as a proximate incident to the conduct of any trade or business in which he was engaged at the time the claim became worthless.

(2) In 1942 A sells the business to C but sells the claim against B to the taxpayer, D. The claim becomes worthless in D's hands in 1943, at a time when D is not engaged in a trade or business incident to the conduct of which a loss from the worthlessness of such a claim would be a proximate result. D's loss is controlled by the non-business debt provisions, even though the original consideration was advanced by A in his trade or business.

(3) In 1942 A dies, leaving the business, including the accounts receivable, to his son, C, the taxpayer. The claim against B becomes worthless in C's hands. C's loss is not controlled by the non-business debt provisions. While C did not advance any consideration for the claim or acquire it in carrying on his trade or business, the loss was sustained as a proximate incident to the conduct



of the trade or business in which he was engaged at the time the debt became worthless.

(4) In 1942 A dies, leaving the business to his son, C, but the claim against B to his son, D, the taxpayer. The claim against B becomes worthless in D's hands in 1943, at a time when D is not engaged in a trade or business incident to the conduct of which a loss from the worthlessness of such claim would be a proximate result. D's loss is controlled by the nonbusiness debt provisions, even though the original consideration was advanced by A in his trade or business.

(5) In 1942 A dies and while his executor, C, is carrying on the business, the claim against B becomes worthless. The loss sustained by A's estate is not controlled by the nonbusiness debt provisions. While C did not advance any consideration for the claim on behalf of the estate or acquire it in carrying on a trade or business in which the estate was engaged, the loss was sustained as a proximate incident to the conduct of the trade or business in which the estate was engaged at the time the debt became worthless.

(6) In 1942, A, in liquidating the business, attempts to collect B's claim but finds that it has become worthless. A's loss is not controlled by the non-business debt provisions, since a loss incurred in liquidating a trade or business is a proximate incident to the conduct thereof.

The provisions of this section with respect to nonbusiness debts are applicable only to taxable years beginning after December 31, 1942.



**United States**  
**COURT OF APPEALS**  
**for the Ninth Circuit**

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SAM SCHNITZER,

ESTATE OF HARRY J. WOLF, Deceased, by  
Monte L. Wolf, Administrator, de bonis non  
with the will annexed of said estate,

MONTE L. WOLF,

BLOSSOM M. GOLDSTEIN,

CHARLOTTE C. COHON,

ESTATE OF JENNIE WOLF, Deceased, by Monte  
L. Wolf, Administrator de bonis non with the  
will annexed of said estate,

*Petitioners,*

vs.

COMMISSIONER OF INTERNAL REVENUE,

*Respondent.*

---

**REPLY BRIEF FOR PETITIONERS**

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On Appeal from the Tax Court of the United States.

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ROBT. T. JACOB and  
JACOB & BROWN,  
*Attorneys for Petitioners.*

GARTHE BROWN,  
*Of Counsel.*



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**REPLY BRIEF FOR PETITIONERS**

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On Appeal from the Tax Court of the United States.

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**RESPONDENT'S POINT II. BUSINESS LOSS**

We shall answer respondent's contention at page 51  
of his brief first. He states:



"Furthermore, should this court hold, contrary to our contention in Point I, *Supra*, that debts did result from the advances, nevertheless they were not business debts and, hence, as provided by Section 23(k)(4) of the Code, are considered as a loss from the sale or exchange of a capital asset held for not more than six months and deductible only at the capital loss rates. (Sec. 117)"

As provided in Section 23, Internal Revenue Code, to be deductible a debt must become worthless within the taxable year. As to the question of worthlessness the court found (R. 51-2 and Resp. Br. 15-6):

"Immediately after the sale the purchasers elected new officers and directors, Mears becoming president. Pursuant to a resolution of the new directors and with the consent of RFC, the corporation gave to Morris, Sam and Rose Schnitzer and Harry J. and Jennie Wolf . . . its 6% note for \$151,000, . . . . .

"By accepting the \$151,000 note in exchange for the two newly made promissory notes, the five former stockholders of Oregon Steel failed to recover \$303,625.90 of the total shown due from the corporation for their advances on open account, which at the time showed credit balances aggregating \$454,625.90. . . . .

"Alaska Junk then charged off \$202,350.60 on its account with the corporation as a bad debt." Also see Exhibit 22, Minutes of Oregon Steel's directors' meeting November 26, 1943, and petitioners' Exhibit 20, cancelled note.)

It is, therefore, clear that the loss occurred in 1943 and was properly recorded in that year. Was it incurred in petitioners' business? Section 29.23(k)(6), Regula-

tion 111, provides in part:

“The question whether a debt is one the loss from the worthlessness of which is incurred in the taxpayer’s trade or business is a question of fact in each particular case. The determination of this question is substantially the same as that which is made for the purpose of ascertaining whether a loss from the type of transaction covered by section 23(e) is ‘incurred in trade or business’ under paragraph (1) of that section.”

The application of Section 23(k) is such that debts are allowable without limitation as deductions if they become worthless as a proximate incident to the business of the taxpayer. Obviously petitioners were engaged in business. The controverted transactions arose in the regular course of petitioners’ business, conducted through Alaska Junk (R. 42).

The last sentence of the second paragraph and the last paragraph of Section 29.23(k) reads:

“ . . . If that relation is a proximate one in the conduct of the trade or business in which the taxpayer is engaged at the time the debt becomes worthless, the debt is not a non-business debt for the purposes of this section.

“To illustrate: A, an individual engaged in the grocery business and who makes his income tax returns on the calendar year basis, extends credit on an open account to B in 1941.”

It will be noted the above provides that if the relation of the debt is “proximate” to the taxpayer’s business at the time the loss occurs it is not a non-business bad debt. Illustrations 1, 2 and 4 in the examples given un-

der Section 29.23(k) show that if the account receivable claimed as a bad debt is separated from the conduct of the creditor's business at the time it becomes worthless, the loss is not sustained as a proximate incident to the conduct of the business, while illustrations 3, 5 and 6 show that if the account remains associated with the business out of which it grew till it becomes worthless, the loss is a proximate incident of the conduct of the business, and hence is an allowable deduction as a bad debt.

It would be redundant to argue further that the loss is controversy was connected with petitioners' business or to cite cases illustrative of that point. The fact is patently obvious.

## **THE ISSUE**

### **ANSWERING RESPONDENT'S ARGUMENT I A**

Respondent's argument (Br. 21 et seq.) is that because the allowance of the questioned deduction is subject to legislative grant, petitioners must seek it "with prayer and supplication". No such aura of sanctity obscures petitioners' rights. It is true that all deductions depend upon "legislative grant", but that grant as to debts is explicit in the taxing act, and to establish their right to the allowance of the claimed loss petitioners are required to do no more than assume the burden of establishing the existence of the debt as a debt and that it became worthless in 1943.

Respondent laborious briefs this point, but none of his argument is applicable to the present controversy, for the rule he defends is one dealing with "statutory" construction. The cases he cites clearly show this. We are concerned here with a factual question. Did the advances create a "debt"? If they did, Section 23(k) says they "*shall* (must) be allowed as deductions" in computing net income. How could the legislative "grace" be more explicit?

Respondent is attempting to convert a rule of statutory construction into a rule for the interpretation of facts. This he may not do. The burden of proof in the case at bar is no different and is no more strict than in any other case.

In dealing with the question of a deduction for obsolescence, the Supreme Court in *Burnet v. Niagara Falls Brewing Co.*, 282 U.S. 648 (1931), said:

" . . . It is a familiar rule that tax laws are to be liberally construed in favor of taxpayers. (Citing cases)

"It would be unreasonable and violate that canon of construction to put upon the taxpayer the burden of proving to a reasonable certainty the existence and amount of obsolescence. Such weight of evidence as would reasonably support a verdict for a plaintiff in an ordinary action for the recovery of money fairly may be deemed sufficient. . . ."

In *National Weeklies v. Commissioner*, 137 F. (2d) 39 (C.C.A. 8th, 1943), the court stated the rule as follows:



“When a taxpayer challenges the factual warrant for a deficiency assessment by the Commissioner, he must produce evidence before the Board of Tax Appeals which reasonably demonstrates that the Commissioner was wrong. *Burnet v. Houston*, 283 U.S. 223, 51 S. Ct. 413, 75 L. Ed. 991; *Lamaghi Coal Co. v. Helvering*, 8 Cir., 124 F. 2d 645; *Clements v. Commissioner*, 8 Cir., 88 F. 2d 791.”

Many of the cases cited by the respondent used language speaking of legislative grant only as embellishment. In many of the other cases cited the *facts were stipulated* and this left for determination only the terms used in the taxing statutes.

In the present case there is no question whether the statute is susceptible of one meaning or another. Its meaning is clear. The tests for analyzing a particular set of facts to determine whether they come within the purview of the statute are also clear. The only question is with respect to the facts.

## **RESPONDENT'S POINT B. RECORD FACTS**

Respondent asserts (Br. 25):

“Taxpayers’ chief reliance is on the testimony of their witnesses at the hearing, especially Morris Schnitzer, that the shareholders never intended to invest more than \$187,800.00 in stock. . . .”

Such is not the case. Petitioners’ brief fully sets forth the facts and circumstances upon which they rely, and among them are (Pet. Br. 11):

“Petitioners’ Business Includes Making Advances as Loans.”



Under this heading it is shown that, as found by the Tax Court, the advances in question were made in connection with a long established business practice followed by Alaska Junk in making such advances "in expectation of maintaining or increasing its trade" (R. 38); that Alaska Junk also made very large advances to enterprises in which petitioners' families were interested; that some of the advances were made as loans and some for the purchase of capital stock; that Alaska Junk always handled these transactions on its books of account as accounts receivable; that Alaska Junk in 1933 had sustained and had been allowed by the Commissioner a deduction on account of a loss from advances made to "a subsidiary", National Machinery Company (R. 198, 292, 360 and Exhibit 56); that the advances to Oregon Steel were made under identical circumstances and exactly in accordance with a practice which had been traditionally followed for thirty years; that there is no evidence of a departure from standard, orthodox practices in making or recording the advances to Oregon Steel; that Oregon Steel recognized the indebtedness and recorded Alaska Junk's vouchers for advances "in exactly the same manner as all other vouchers or invoices . . ." (R. 452). "All accounts (after entries for stock issued and debentures had been placed on the books) would be current and would be paid either out of RFC funds of operating profits." (Testimony Leon D. Margosian, certified public accountant, R. 258); that the account remained on the books of both the debtor and the creditor until it was compromised and settled in November, 1943, by the issuance of a third mortgage

note; that the settlement with both creditors, Alaska Junk and Morris Schnitzer, was made upon the basis of the indebtedness of Oregon Steel as shown by its open account payable to the respective parties, and not in proportion to the amount of stock held by each.

All of these facts clearly and affirmatively reflect the existence of the debtor-creditor relationship, and neither the trial court nor respondent pointed to a single affirmative, positive, evidentiary fact which indicates any other intention on the part of the petitioners of Oregon Steel.

Under point II, 2 (Br. 23-28) petitioners also showed that the evidentiary facts as found by the Tax Court require the ultimate finding the advances were intended to and did create the debtor-creditor relationship.

Petitioners further showed (Br. 28-38) that, contrary to the Tax Court's views, the documentary evidence relied upon as a basis for its adverse inferences does not support the inferences that were adopted.

### **Point 1 (Resp. Br. 27)**

The rule urged by respondents that the mere naming of a thing is not conclusive, is a true one. However, all of the circumstances, including the name applied, are to be considered in making the determination. It is to be noted that taxpayers were consistent in the naming.

The Tax Court found that the refusal of taxpayers to *invest* more than \$250,000 (a fortiori \$187,000) was the cause of their difficulty in securing outside financing

(R. 65). Had they had any *intention* of ever increasing the invested capital it would have been to their greatest advantage to have done so then, but they did not. They steadfastly refused to ever increase either the *authorized* or the *invested* capital, preferring to meet the obligations by advances continuously characterized as loans.

The reasons for their refusal were adequately explained by Morris Schnitzer. He promoted the project (R. 87). He wanted to keep control (R. 83). If the subscribed capital had been increased he would have lost control.

The Tax Court and respondent make much of the fact that the advances made were used for investment in corporate organization and plant, and by "their very nature (were) placed at the risk of the business". Surely, it cannot be seriously contended that the use of the money has any effect upon the nature of the advance. All of the funds from RFC, bank loans and \$190,000.00 advanced by outside creditors, were used for organization and plant, but that fact does not alter the character of the advances by these creditors.

### **Point 2 (Resp. Br. 27)**

Respondent undertakes to brush aside as meaningless petitioners' practice of charging advances to debtors as "accounts receivable", notwithstanding the fact the practice had been followed for thirty years. And in spite of the fact they represent and are in accordance with the standard, orthodox practice of handling such trans-

actions. The fact the charges were in three categories in no way changes the legal effect of the debtor's obligation. They were all charges to the vendee, and nothing would have been added by making charges to three separate accounts receivable.

### **Point 3 (Resp. Br. 28)**

Respondent raises the point that no interest was charged and no written evidence of indebtedness was issued to cover the advances. This might be a significant fact, except for two things. While interest and formal written evidence of indebtedness are indicia of indebtedness, it cannot be argued that a debt does not exist or is not a debt simply because interest is not charged or accrued, or that no evidence of indebtedness was issued. Further, this was not an isolated transaction. It was one of many similar transactions wherein taxpayer made advances to various enterprises (R. 38-40). There is not one scintilla of evidence of interest ever having been charged in any of those transactions, except Hesse Ersted Company (R. 236). No question has ever been raised as to the intent of the parties in those transactions to create a debt and from the evidence we can but deduce that the surrounding facts were identical; no interest charge, no written evidence of indebtedness except the open book account, no date certain for payment, etc. Petitioners were engaged in the business of making loans, but were not so engaged for a direct profit on the loan. Their purpose was to create good will, to help in starting new businesses as prospective customers of



their business, and to encourage new or growing present customers to trade or continue to trade with them. It is significant that these previous loans were repaid by supplying merchandise and scrap, and seldom in cash (R. 234-238, 302-308).

#### Point 4 (Resp. Br. 29)

Respondent complains that no notes except those dated November 26, 1943, were given.

(a) It is well known that in trade it is not the practice to execute notes for trade accounts, and it is axiomatic that this is not necessary to create an indebtedness.

(b) Nor is corporate action necessary in ordinary, everyday business transactions, such as those involved here, in order to create a subsisting liability. As early as 1924 the Board of Tax Appeals (now Tax Court) held in the appeal of *Rube Isaac & Co.*, 1 B.T.A. 45, that closely held corporations act very much like partnerships and that any acts of the corporation

“ . . . pursuant to oral understanding are as binding as though sanctified by the most rigid adherence to legal formality, . . . (Citing cases.”

Nor is it necessary to fix an absolute date of maturity. However, in the instant case, as testified by Leon Margosian

“I was instructed . . . all other accounts would be current and would be paid either out of RFC funds or operating profits.” (R. 453)

The accounts were to be repaid currently.



### Point 5 (Resp. Br. 29)

Here respondent dwells upon what he terms a strict rule of construction. Petitioners are well aware, as has been set out above, that they must show that a debt existed and that it became worthless, but Congress has specifically provided for the deduction of all losses resulting from debts becoming worthless, and the degree of proof required here is no greater than that required with respect to such items as interest, expenses, depreciation, taxes and any other such items provided for in the revenue act. This is a "business deduction", and the transactions that are the subject matter of the loss were ordinary and necessary business transactions. Therefore, they must be viewed in that light. To require more would be to place an unnecessary burden and penalty upon legitimate business operations. These debts were created out of profit producing transactions entered into at arms length, including the sale of merchandise at the regular going prices to the trade, and petitioners have paid Federal incomes taxes upon the profits made from said transactions. It would be a harsh rule indeed for the government to apply one standard of construction against a taxpayer in obtaining taxable profit upon such transactions, and to apply a stricter standard in depriving the same taxpayer of the loss sustained in connection with the identical transactions.

The chronological sequence of events set forth by respondent is very helpful and significant. He continually talks of ambiguities of taxpayers' dealings, but it

should be apparent to this court that far from being ambiguous they are consistently and clearly indicative of the intent to create a debt. *Certificate of Contributions Of Capital* (Ex. Q), clearly shows intent to create a debt. Respondent makes much of the words "contributed capital" but his argument shows a complete lack of careful analysis. While vigorously urging the rule that parties cannot rely on words of art for their technical meaning, but must look to legal effect, he completely ignores his own warnings. The certificate states Petitioners *had* (note the use of the past tense) "contributed capital" of \$299,069.70, and that Morris Schnitzer *had* "contributed capital" of \$138,984.11, and, most significantly, continues:

" . . . that there will be issued to such contributors, . . . common stock in said corporation at par in the sum of \$187,700, *and the balance* in the debentures of said corporation. . . ." (Italics supplied)

Respondent asks this court to infer Morris Schnitzer, by use of the words "contributed capital", is inconsistent with his testimony the parties did not intend to invest more than \$187,700. A careful reading clearly shows that Morris Schnitzer included in "contributed capital" both investment and debt, and the ordinary meaning of the words "contributed capital" must be tempered by their obvious use to embrace both investment and debt, as is clearly set forth in the body of the instrument. Contrary to respondent's attempt to use this exhibit to impeach Morris Schnitzer's testimony as to intent, it, in fact, substantiates it.

The significance of the balance of the instrument was to reassure RFC its loan would at all times be paramount to all advances made by the incorporators.

Exhibit R referred to by respondent is in the same terminology and by its terms it, too, specifically defines "contributed capital" and the phrase "contributed as capital investment" as including investment and debt. Thus, again, no significance to the terms can be given outside the obvious meaning contained in the entire instruments.

Counsel's attempt to minimize the importance of the actual repayment by RFC of \$114,519 on the debt emphasizes the significance of the fact. An actual repayment of \$114,519 on the total debt was made. The fact stands as a beacon light.

Counsel (Br. 14) would regard as significant the fact at the time debentures were issued, they were not issued for the full amount of the open account outstanding. The simple fact is, a debt is a debt. The issuance of debentures would not change an investment into a debt. No allocation of this open account was needed. A debt without security is nonetheless a debt, and counsel's shock at a failure to take debentures for the balance of the account did not change its essential character as a debt.

In counsel's speculation as to Petitioners' intent to withhold any designation of the advances awaiting their best advantage (Br. 41) he is laboring without benefit of evidence.

Every act and deed, every word spoken or written prior to the collapse of Oregon Steel indicates an abiding intention to regard these advances over the amount of the authorized capital as debt. There are only failing inferences to the contrary. Petitioners steadfastly refused to convert their loans to investment, notwithstanding the refusal of Commercial Credit Corporation, Bank of America, Bank of Portland and New York Investment houses to advance capital unless they did so (R. 43). These are "record facts" and not testimony given five years after the transactions.

It is difficult to see how counsel or the Tax Court could find any intent other than to create a debt in view of these facts. One's declaration as to a fact made at a time when his then best interest lies contrary to such a declaration is one that simply cannot be overcome.

Counsel's Point 6 (Br. 43) is fully answered in Petitioners' brief, pages 42-45.

## **PETITIONERS MUST SHOW THAT TRIER'S FINDING WAS ERRONEOUS**

As to respondent's argument that petitioners must show the trial court's findings that the advances did not create a debt is "clearly erroneous", petitioners assume that burden. The problem is: When is a finding "clearly erroneous?" We have it on the highest authority, *United States v. U. S. Gypsum Company*, 333 U.S. 364 (1948), that a finding is clearly erroneous when, although there is evidence to support it, on the *entire record* the re-



viewing court is left with the firm conviction a mistake has been committed. Neither the Tax Court nor respondent points to a single cogent, convincing fact upon which to bottom the inferences leading to the court's ultimate findings or conclusions, and *this court need not go outside of the trial court's own detailed evidentiary findings to discover the error it committed*. The primary facts found contain all essential elements of a debtor-creditor relationship, and the court points to no affirmative, positive, unorthodox act connected with the condemned transactions, even in the light of the most rigid income tax standards, which, upon impartial analysis, shows any thought or intention by petitioners to treat the advances other than as accounts receivable which they expected to be repaid.

The debtor-creditor relationship does not depend upon fixed indicia, such as notes, interest, corporate action authorizing purchase of merchandise or receipt of advances, but depends upon normal indicia applicable to individual situations.

The court's inferences are strained, illogical and do not conform to a natural, rational interpretation applicable to regular, standard, orthodox business transactions. The essential question is whether the debtor-creditor relationship was created by the sales of merchandise and the advances made to Oregon Steel. The evidence is clear that not only petitioners but Oregon Steel intended to create a debt.

Regarding respondent's reference to corporate liabilities, capital stock, use of the funds, adequacy of cor-



porate capital, payment of interest, payment of advances from corporate profits, etc., none of these conditions is determinative of the question, none is recognized by the courts as determinative criteria, but as petitioners point out, page 45-49 of their brief, the **SOLE** criterion followed in the cases is the "intent of the parties", and only insofar as relevant facts bear upon that point are they of help in determining the issue. Respondent seeks to draw the attention of the court away from the primary facts. We have a clear statement of the evidentiary facts upon which to ground the ultimate findings. The court forsakes the preponderant facts and magnifies insignificant circumstances considered as rebutting them.

On the question of when findings are "clearly erroneous" Judge Orr struck at the heart of the problem in *Wilshire and Western Sandwiches, Inc. v. Commissioner*, 175 F. (2d) 718, in the following language:

"Petitioner asserts that the transactions under consideration here have few of the characteristics of the people dealing at arms length. Whatever view may be taken as to the number of those characteristics, the *controlling fact remains* that those which appear are the essentials of a bona fide transaction. In reaching this conclusion we think we are dealing with substance and reality and not mere form, a requirement in the field of taxation." (Italics supplied)

Whatever inference may have been drawn by the trial court the "controlling facts" here are that for thirty years petitioners had been engaged in a business which included making advances to other persons for "maintaining or increasing its trade"; in June, 1941 more than

four months before any advances were made to Oregon Steel petitioners fixed the amount of stock they intended to subscribe; the books of all parties *consistently* recorded the advances under a debtor-creditor classification; these accounts remained as originally entered until the obligations were compromised and written off as bad debts.

While it is true Rule 52 FRCP contemplates that in appraising oral testimony the appeal court must give "due regard . . . to the opportunity of the trial court to judge of the credibility of the witnesses", nevertheless, as stated by this court in *Grace Bros., Inc. v. Commissioner*, 173 F. (2d) 173, "it is axiomatic that uncontradicted testimony must be followed" and there is no exception to this rule unless the witnesses stand impeached and the impeachment is conjoined with contradictory testimony, physical facts *actually proved*, or the testimony is inherently improbable. It is noteworthy that respondent does not attempt to show that the testimony of petitioners' witnesses was contradicted by other testimony, or "by facts actually proved", but he mildly suggests (Br. 26):

"The Tax Court did not err in declining to accept testimony . . . which in the light of the entire record *might reasonably be regarded* as inherently improbable." (Italics supplied)

This falls far short of justifying the Tax Court in arbitrarily disregarding this uncontradicted testimony, and constitutes plain error, as is so aptly expressed in *Lawton v. Commissioner*, 164 F. (2d) 380 (C.C.A. 6th,

1947), and *Grace Bros., Inc. v. Commissioner*, 173 F. (2d) 170 (C.C.A. 9th, 1949). This rule is not relaxed by the fact the witnesses were friendly. Perjury is perjury and truth is truth, whether from the lips of friendly or adverse witnesses.

Such cases as *Aetna Life Insurance Co. v. Kepler*, 116 F. (2d) 1 (C.C.A. 8th, 1941), quoting William D. Mitchell, Chairman of Advisory Committee for revision of FRCP; *Fleming v. Palmer*, 123 F. (2d) 749 (C.C.A. 1st, 1941); *Murray v. Noblesville Milling Co.*, 131 F. (2d) 470, 474 (C.C.A. 7th, 1942); *Presidio Mining Co. v. Overton*, 270 Fed. 388 (C.C.A. 9th, 1921), are authority for the rule that if ultimate findings by the trier are contrary to the clear weight of evidence or the preponderance of the evidence they are clearly erroneous.

The evidentiary facts found by the court meet the requirement laid down by *Lawton v. Commissioner*, *supra*, in that they "lend a flavor of truthfulness to their assertions". Consequently, this testimony may not be disregarded but "*must be followed*".

## THE DOCTRINE OF STARE DECISIS

In *Wilshire & Western Sandwiches, Inc. v. Commissioner*, *supra*, and *Maloney v. Spencer*, 172 Fed. (2d) 638, the court has held that "intent" of the parties with respect to transactions such as those involved in this appeal is controlling. To decide otherwise in this case would be contrary to that rule.

See *Jorgensen v. Swope*, 114 F. (2d) 988 (C.C.A. 9th, 1940), in which the trial court followed its previous decision in *Cooke v. Swope*, and stated:

“ . . . The decision of the trial judge in *Cooke v. Swope*, *supra*, was sustained by this court. 9 Cir., 109 F. 2d 955. Our decision in that case should be followed unless there is some controlling distinction or some subsequent decision by the Supreme Court requiring us to depart therefrom. There are none.”

Also in *Papani v. United States*, 84 F. (2d) 160 (C.C.A. 9th, 1936), unlawful search was involved and this court said:

“ . . . However, this court has determined that such statements are not always conclusive, but must be considered with the other actions of the officers, and the surrounding circumstances (Citing cases). Such rule, under the doctrine of stare decisis, is controlling with respect to this court.”

## CONCLUSION

The Tax Court's decisions were clearly erroneous and should be reversed.

Respectfully submitted,

ROBT. T. JACOB,  
JACOB & BROWN,  
Attorneys for Petitioners.

GARTHE BROWN,  
Of Counsel.

No. 12477

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United States  
Court of Appeals  
for the Ninth Circuit.

---

MARY ZELLMER, as Administratrix of the Estate of Orval Zellmer and MAY ZELLMER, an Individual,

Appellant,

vs.

ACME BREWING CO., a Corporation,

Appellee.

---

Transcript of Record

---

Appeal from the United States District Court  
Northern District of California,  
Southern Division

FILED  
APR 6 1959

PAUL P. O'BRIEN





No. 12477

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United States  
Court of Appeals  
for the Ninth Circuit.

---

MARY ZELLMER, as Administratrix of the Estate of Orval Zellmer and MAY ZELLMER, an Individual,

Appellant,

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Transcript of Record

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Appeal from the United States District Court  
Northern District of California,  
Southern Division



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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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## NAMES AND ADDRESSES OF ATTORNEYS

BRUCE WALKUP,

DAN L. GARRETT, JR.,

410 Mills Building,

San Francisco, California,

Attorneys for Plaintiff and Appellant.

BRONSON, BRONSON and McKINNON,

Mills Tower,

San Francisco, California,

Attorneys for Defendant and Appellee.

In the United States District Court for the Northern District of California, Southern Division

No. 29034G

MARY ZELLMER, as Administratrix of the Estate of ORVAL ZELLMER; and MARY ZELLMER, an Individual,

Plaintiff,

vs.

ACME BREWING CO., a Corporation, FIRST DOE, SECOND DOE, THIRD DOE, FIRST DOE COMPANY, SECOND DOE COMPANY, and THIRD DOE COMPANY,

Defendants.

### COMPLAINT FOR WRONGFUL DEATH AND BREACH OF WARRANTY

Plaintiff complains of defendants and for her first claim alleges that:

#### I.

Defendants, First Doe, Second Doe, Third Doe, First Doe Company, Second Doe Company, and Third Doe Company, are sued herein by said names, which are fictitious, for the reason that plaintiff does not know the true names of said defendants, and plaintiff prays leave that when said true names are ascertained, plaintiff may amend this complaint to set forth said true names, together with appropriate charging allegations.

II.

On February 21, 1949, Mary Zellmer was duly appointed Administratrix of the estate of Orval Zellmer, deceased, in the Second Judicial District Court of the State of Nevada, in and for the County of Washoe. Thereafter, and on June 15, 1949, Mary Zellmer duly qualified as such Administratrix and Letters of Administration were duly issued to her on June 15, 1949, by the said Second Judicial District Court of the State of Nevada, in and for the County of Washoe.

III.

At all times mentioned herein, defendant, Acme Brewing Co., was a corporation, organized and existing under and by virtue of the laws of the State of California, and was doing business in the Northern District of California.

IV.

At all times mentioned herein, Mary Zellmer was and now is a resident of the State of Nevada.

V.

From on or about January 18, 1944, Mary Zellmer and Orval Zellmer, her husband, were the owners and operators of the Red Feather Bar and Restaurant, located in the Town of Wadsworth, County of Washoe, State of Nevada.

VI.

On or about October 10, 1947, Mary Zellmer and her husband, the said Orval Zellmer, purchased

twenty-five cases of beer from the Shoshone Coca-Cola Bottling Co. of Reno, Nevada. The said twenty-five cases of beer were manufactured by defendant, Acme Brewing Co., and distributed through and by the said Shoshone Coca-Cola Bottling Co. in Reno, Nevada.

#### VII.

On or about November 30, 1947, at Wadsworth, County of Washoe, State of Nevada, the said Orval Zellmer opened one of the bottles of Acme Beer from said twenty-five cases of beer, and Mary Zellmer and the said Orval Zellmer each drank part of the contents thereof.

#### VIII.

After Orval Zellmer and Mary Zellmer drank said beer as aforesaid, they discovered that said bottle contained a dead mouse. The said mouse was present in said bottle due to the careless and negligent manufacture of said beer by defendant, Acme Brewing Co., rendering said beer unfit for human consumption and dangerous and injurious to human life.

#### IX.

As a direct and proximate result of defendant's negligent and careless manufacture of said bottle of beer, Orval Zellmer became violently ill and thereafter died on or about February 25, 1948, at Wadsworth, County of Washoe, State of Nevada.

#### X.

As a direct and proximate result of defendant's

negligent and careless manufacture of said bottle of beer, the estate of Orval Zellmer, deceased, became liable for medical and funeral expenses in the amount of \$954.00.

## XI.

As a direct and proximate result of defendant's negligence aforesaid, which directly and proximately caused the death of said Orval Zellmer, plaintiff, as Administratrix of the estate of Orval Zellmer, has been damaged generally in the amount of \$120,000.00.

Wherefore, plaintiff prays judgment as hereinafter requested.

And for a Second and Separate Claim, plaintiff alleges that:

### I.

Plaintiff repleads and incorporates herein by reference paragraphs I, II, III, IV, V, VI, VII, and VIII of plaintiff's first claim.

### II.

The presence of said mouse in said bottle of Acme Beer constituted a breach by defendant, Acme Brewing Co., of an implied warranty of fitness for the purpose for which said beer was sold by defendant, and rendered the said bottle of beer unfit for human consumption and dangerous and injurious to human life.



## III.

As a direct and proximate result of defendant's breach of warranty as aforesaid, Orval Zellmer became violently ill and thereafter died on or about February 25, 1948, at Wadsworth, County of Washoe, State of Nevada.

## IV.

As a direct and proximate result of defendant's breach of warranty as aforesaid, which directly and proximately caused the death of Orval Zellmer, the estate of Orval Zellmer became liable for medical and funeral expenses in the amount of \$954.00.

## V.

As a direct and proximate result of defendant's breach of warranty as aforesaid, which directly and proximately caused the death of said Orval Zellmer, plaintiff, as Administratrix of the estate of Orval Zellmer, has been damaged generally in the amount of \$120,000.00.

Wherefore, plaintiff prays judgment as hereinafter requested.

And for a Third and Separate Claim, plaintiff alleges that:

## I.

Plaintiff repleads and incorporates herein by reference paragraphs I, III, IV, V, VI, VII of plaintiff's first claim.

## II.

The presence of said mouse in said bottle of

Acme Beer constituted a breach by defendant, Acme Brewing Co., of an implied warranty of fitness for the purpose for which said beer was sold by defendant and rendered the said bottle of beer unfit for human consumption and dangerous and injurious to human life.

### III.

As a direct and proximate result of defendant's breach of warranty as aforesaid, plaintiff became violently ill, and suffered severe internal strain and injuries from repeated and prolonged periods of vomiting and was unable to consume normal food for more than one month, and was rendered sick, sore, and disabled and confined to her home for more than three months, and suffered great and irreparable physical damages.

### IV.

Plaintiff is informed and believes and therefore alleges upon such information and belief that she has suffered permanent mental damages which will partially incapacitate her from earning her livelihood and will require future medical care and services for many years, and that she has been damaged generally in the amount of \$100,000.00.

Wherefore, plaintiff prays judgment as follows:

1. On her first claim for the sum of \$120,954.00.
2. On her second claim for the sum of \$120,-954.00.
3. On her third claim for the sum of \$100,000.00.

4. For her costs of suit incurred herein, and

5. For such other and further relief as the Court shall deem proper.

/s/ BRUCE WALKUP,

Attorney for Plaintiff.

(Endorsed): Filed Jul. 29, 1949.

[Title of District Court and Cause.]

### MOTION TO DISMISS

Defendant, Acme Brewing Co., a corporation, moves the Court to dismiss the complaint herein on the grounds that it appears from the face of the complaint that the cause of action set up in said complaint did not accrue, if it accrued at all, within one year before the bringing of this suit.

Said motion will be based on this written motion, notice of motion, the memorandum of points and authorities filed herewith and upon all of the records, documents and papers on file in the above-entitled action.

Submitted herewith is a draft of the order proposed and requested by said defendant.

Dated: September 22, 1949.

BRONSON, BRONSON &  
McKINNON.

/s/ E. D. BRONSON,

/s/ NORMAN A. EISNER,

Attorneys for Defendant, Acme Brewing Co., a Corporation.

NOTICE OF MOTION TO DISMISS

To Plaintiff Above Named and to Messrs. Bruce Walkup and Dan L. Garrett, Jr., Her Attorneys:

You and Each of You Will Please Hereby Take Notice that defendant, Acme Brewing Co., a corporation, will bring the above motion for hearing in the above-entitled Court before the Honorable Louis E. Goodman, on the 3rd day of October, 1949, at the hour of 10:00 o'clock a.m. of said day or as soon thereafter as counsel may be heard at the courtroom of the above-entitled Court, located in the Post Office Building, Seventh and Mission Streets, San Francisco, California.

Dated: September 22, 1949.

BRONSON, BRONSON &  
McKINNON.

/s/ E. D. BRONSON,

/s/ NORMAN A. EISNER,

Attorneys for Defendant, Acme Brewing Co., a Corporation.

[Endorsed]: Filed Sept. 23, 1949.

[Title of District Court and Cause.]

### ORDER OF DISMISSAL

The motion of defendant, Acme Brewing Co., a corporation, to dismiss the complaint on file herein having come on regularly this day for hearing, and the Court being fully advised and finding that the complaint on file was filed more than one year after the cause of action, if any, accrued to the plaintiff herein,

It Is Hereby Ordered that said complaint be, and it hereby is dismissed.

Dated: October . . . ., 1949.

.....,

Judge of the District Court.

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[Title of District Court and Cause.]

### ORDER GRANTING MOTION TO DISMISS

Defendant's motion to dismiss is granted.

Dated: December 28, 1949.

/s/ LOUIS GOODMAN,  
U. S. District Judge.

[Endorsed]: Filed Dec. 28, 1949.



In the United States District Court for the Northern District of California, Southern Division

No. 29034-G

MARY ZELLMER, as Administratrix of the Estate of ORVAL ZELLMER; and MARY ZELLMER, an Individual,

Plaintiff,

vs.

ACME BREWING CO., a Corporation, FIRST DOE, SECOND DOE, THIRD DOE, FIRST DOE COMPANY, SECOND DOE COMPANY, and THIRD DOE COMPANY,

Defendants.

### ORDER OF DISMISSAL

Defendant's motion to dismiss having come on regularly for hearing, and this court after oral and written argument by plaintiff and defendant granted defendant's motion to dismiss on December 28, 1949. It is hereby ordered that plaintiff's complaint on file herein, and each cause of action therein, be and the same is hereby dismissed, and the clerk is hereby directed to enter this dismissal of record.

Dated: January 20, 1950.

/s/ LOUIS GOODMAN,  
U. S. District Judge.

[Endorsed]: Filed January 23, 1950.

[Title of District Court and Cause.]

### NOTICE OF APPEAL

Mary Zellmer, as Administratrix of the Estate of Orval Zellmer, and Mary Zellmer, an individual, plaintiffs above named, hereby appeal to the Court of Appeals for the Ninth Circuit from the Order of Dismissal of the above-entitled Court whereby plaintiffs' complaint on file herein and each cause of action therein was ordered dismissed on January 20, 1950. Said order being entered in this action on January 21, 1950.

BRUCE WALKUP,  
DAN L. GARRETT, JR.

By /s/ DAN L. GARRETT, JR.,  
Attorneys for Appellants.

[Endorsed]: Filed Feb. 1, 1950.

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[Title of District Court and Cause.]

### NOTICE DESIGNATING CONTENTS OF RECORD ON APPEAL

To the Clerk of the United States District Court  
for the Northern District of California, Southern  
Division:

You are hereby requested to prepare the record on appeal in the above-entitled action and to include in such record, plaintiff's complaint filed herein on July 29, 1949; defendant's Motion to Dismiss

and Notice of Motion to Dismiss filed herein on or about September 22, 1949; the Order of the above-entitled Court granting defendant's motion to dismiss dated December 28, 1949, and filed herein December 28, 1949; the Order of the above-entitled Court dismissing plaintiff's complaint on file herein, dated January 20, 1950, and filed herein on January 21, 1950; plaintiff's Notice of Appeal filed herein on or about January 31, 1950; plaintiff's Statement of Points Relied on on Appeal and plaintiff's Notice Designating Contents of Record on Appeal.

Dated: February 1, 1950.

BRUCE WALKUP,  
DAN L. GARRETT, JR.,

By /s/ DAN L. GARRETT, JR.,  
Attorneys for Plaintiff.

[Endorsed]: Filed Feb. 3, 1950.

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[Title of District Court and Cause.]

STATEMENT OF POINTS RELIED ON  
ON APPEAL

Notice is hereby given that plaintiff relies on the following points on appeal in the above-entitled action:

1. Plaintiff's first and second claims are not barred by the statute of limitations contained in

the California Code of Civil Procedure, Section 340, Subsection 3, which prescribes a one-year period within which to file an action for wrongful death.

2. Plaintiff's first and second claims are controlled by the statute of limitations prescribed in Section 5 of Chapter 4 of the Civil Practice Act of 1911, of the State of Nevada for the reason that the said Nevada statute of limitations is substantive in nature and inheres in plaintiff's claims when filed in California.

3. Plaintiff's third claim is not barred by the statute of limitations prescribed by the California Code of Civil Procedure, Section 340, Subsection 3, but is controlled by the statute of limitations prescribed in the California Code of Civil Procedure, Section 339, Subsection 1.

4. If plaintiff's third claim is not controlled by the statute of limitations prescribed in the California Code of Civil Procedure, Section 333, Subsection 1, it is controlled by the statute of limitations prescribed in the California Code of Civil Procedure, Section 343.

BRUCE WALKUP,  
DAN L. GARRETT, JR.,

By /s/ DAN L. GARRETT, JR.,  
Attorneys for Plaintiff.

[Endorsed]: Filed February 3, 1950.

[Title of District Court and Cause.]

CERTIFICATE OF CLERK TO RECORD  
ON APPEAL

I, C. W. Calbreath, Clerk of the District Court of the United States for the Northern District of California, do hereby certify that the foregoing documents, listed below, are the originals filed in this Court in the above-entitled case, and that they constitute the Record on Appeal herein, as designated by the appellant, to wit:

Complaint for Wrongful Death and Breach of Warranty.

Motion to Dismiss and Notice of Motion to Dismiss.

Order Granting Motion to Dismiss.

Order of Dismissal.

Notice of Appeal.

Notice Designating Contents of Record on Appeal.

Statement of Points Relied on on Appeal.

In Witness Whereof, I have hereunto set my hand and affixed the seal of said District Court this 7th day of February, A.D. 1950.

C. W. CALBREATH,  
Clerk.

[Seal] By /s/ M. E. VAN BUREN,  
Deputy Clerk.



[Endorsed]: No. 12477. United States Court of Appeals for the Ninth Circuit. Mary Zellmer, as Administratrix of the Estate of Orval Zellmer and May Zellmer, an Individual, Appellant, vs. Acme Brewing Co., a Corporation, Appellee. Transcript of Record. Appeal from the United States District Court for the Northern District of California, Southern Division.

Filed February 7, 1950.

/s/ PAUL P. O'BRIEN,  
Clerk of the United States Court of Appeals for the  
Ninth Circuit.

In the United States Circuit Court of Appeals  
for the Ninth Circuit

No. 12477

MARY ZELLMER, as Administratrix of the Es-  
tate of ORVAL ZELLMER; and MARY  
ZELLMER, an Individual,

Plaintiff,

vs.

ACME BREWING CO., a Corporation, FIRST  
DOE, SECOND DOE, THIRD DOE, FIRST  
DOE COMPANY, SECOND DOE COM-  
PANY, and THIRD DOE COMPANY,

Defendants.

DESIGNATION OF RECORD MATERIAL  
TO CONSIDERATION OF APPEAL

Appellant herewith designates the entire record  
as material to the consideration of the appeal  
herein.

Dated: February 14, 1950.

BRUCE WALKUP,  
DAN L. GARRETT, JR.,

By /s/ DAN L. GARRETT, JR.,  
Attorneys for Appellant.

[Endorsed]: Filed February 16, 1950.

[Title of U. S. Court of Appeals and Cause.]

## DESIGNATION OF POINTS RELIED ON ON APPEAL

Notice is hereby given that appellant relies on the following points on appeal in the above-entitled action:

1. Appellant's first and second claims are not barred by the statute of limitations contained in the California Code of Civil Procedure, Section 340, Subsection 3, which prescribes a one-year period within which to file an action for wrongful death.

2. Appellant's first and second claims are controlled by the statute of limitations prescribed in Section 5 of Chapter 4 of the Civil Practice Act of 1911, of the State of Nevada for the reason that the said Nevada statute of limitations is substantive in nature and inheres in appellant's claims when filed in California.

3. Appellant's third claim is not barred by the statute limitations prescribed by the California Code of Civil Procedure, Section 340, Subsection 3, but is controlled by the statute of limitations prescribed in the California Code of Civil Procedure, Section 339, Subsection 1.

4. If appellant's third claim is not controlled by the statute of limitations prescribed in the California Code of Civil Procedure, Section 333, Sub-

section 1, it is controlled by the statute of limitations prescribed in the California Code of Civil Procedure, Section 343.

Dated: February 14, 1950.

BRUCE WALKUP,  
DAN L. GARRETT, JR.,

By /s/ DAN L. GARRETT, JR.,  
Attorneys for Appellant.

[Endorsed]: Filed February 16, 1950.

Affidavits of Service by Mail attached.





No. 12,477

IN THE

United States  
Court of Appeals

For the Ninth Circuit

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MARY ZELLMER, as Administratrix of the  
Estate of Orval Zellmer and MARY  
ZELLMER, an Individual,

*Appellant,*

VS.

ACME BREWING Co., a Corporation,

*Appellee.*

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Appellant's Opening Brief

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FILED

APR 10 1950

AUL P. O'BRIEN,  
CLERK

BRUCE WALKUP,  
DAN L. GARRETT, JR.,  
410 Mills Building,  
San Francisco 4, California,  
*Attorneys for Appellant.*



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IN THE  
United States  
Court of Appeals  
For the Ninth Circuit

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MARY ZELLMER, as Administratrix of the  
Estate of Orval Zellmer and MARY  
ZELLMER, an Individual,

*Appellant,*

vs.

ACME BREWING Co., a Corporation,

*Appellee.*

---

Appellant's Opening Brief

---

- I. **STATEMENT OF PLEADINGS AND FACTS SHOWING THE JURISDICTION OF THE UNITED STATES DISTRICT COURT AND THE UNITED STATES COURT OF APPEALS.**
- A. **The United States District Court Had Jurisdiction Over This Suit by Reason of the Diversity of Citizenship of the Parties Hereto, and Because the Claims of Plaintiff and Appellant Herein Were Each in Excess of Three Thousand (\$3,000) Dollars.**

The allegations of the complaint filed in the District Court on July 29, 1949, stand uncontroverted herein inso-

far as allegations necessary to establish the jurisdiction of the District Court are concerned. The complaint alleges in Paragraph III of the first claim therein that "At all times mentioned herein, defendant, Acme Brewing Co., was a corporation, organized and existing under and by virtue of the laws of the State of California, and was doing business in the Northern District of California" (Tr. of Rec. 3).

In Paragraph IV of said first claim it is alleged that "At all times mentioned herein, Mary Zellmer was and now is a resident of the State of Nevada" (Tr. of Rec. 3).

These allegations are incorporated and repleaded by Paragraph I of the second claim of said complaint (Tr. of Rec. 5) and again by Paragraph I of the third claim of said complaint (Tr. of Rec. 6).

Reference to the prayer for damages of the said complaint shows that on each of the three claims joined in said complaint, plaintiff and appellant herein prays judgment in excess of Three Thousand Dollars (\$3,000.00) (Tr. of Rec. 7, 8).

The jurisdiction of the United States District Court therefore arises by virtue of Title 28, United States Code 1332, which states:

"(a) The district courts shall have original jurisdiction of all civil actions where the matter in controversy exceeds the sum or value of \$3,000 exclusive of interest and costs, and is between:

(1) Citizens of different States:"

The United States District Court for the Northern District of California, Southern Division, was furthermore the proper Court insofar as the question of venue is con-

cerned, by virtue of Title 28, United States Code 1391(c), which states:

“(c) A corporation may be sued in any judicial district in which it is incorporated or licensed to do business or is doing business, and such judicial district shall be regarded as the residence of such corporation for venue purposes.”

**3. The United States Court of Appeals for the Ninth Circuit Has Jurisdiction to Review the Order of the United States District Court by Reason of the Fact That Said Order Was a Final Decision.**

On September 23, 1949, defendant and appellee filed its Motion to Dismiss (Tr. of Rec. 8). On December 28, 1949, the United States District Court made its Order granting the said Motion to Dismiss (Tr. of Rec. 10). This Order was followed on January 23, 1950, by an Order of Dismissal by which the United States District Court ordered that:

“\* \* \* plaintiff's complaint on file herein, and each cause of action therein, be and the same is hereby dismissed, and the clerk is hereby directed to enter this dismissal of record.” (Tr. of Rec. 11).

This Order by dismissing the complaint and each cause of action therein terminated finally all rights of plaintiff and appellant herein in the United States District Court. It is from this Order that appellant filed her Notice of Appeal (Tr. of Rec. 12).

The United States Court of Appeals for the Ninth Circuit has jurisdiction to review this Order by virtue of Title 28, United States Code 1291, which specifically confers jurisdiction to review all final decisions of the

(2) The District Court erred in ordering plaintiff's third claim dismissed.

#### IV. ARGUMENT

The ultimate question raised by this appeal, with regard to appellant's first and second claims, is whether or not the Statute of Limitation on actions for wrongful death provided by the law of the forum is a bar to the suit when the cause of action still exists under the Statute of Limitations of the state where the death occurred. There is no decision by California courts on this exact point. The Federal court is therefore free to determine the question for itself (*Calvin v. West Coast Power Co.* (1942) 44 Fed. Supp. 783, 788).

When the time limitation set up by the state where the death occurs is a substantive part of and is inherent in the right to recover for a wrongful death, Federal courts, when free to decide the question for themselves, have uniformly applied the limitation of the state where the death occurred, even though the action would be barred had the death occurred in the state where suit was filed.

##### **A. The Nevada Statute of Limitations on Actions for Wrongful Death Is a Substantive Part of the Right to Sue for Wrongful Death Granted by the State of Nevada, and Accompanies That Right Wherever Enforcement of It Is Sought.**

The test for determining whether or not such a time limitation, as is here involved, is a matter of substance or a matter of procedure alone was set out by Mr. Justice Holmes in *Davis v. Mills* (1904) 194 U.S. 451; 24 Sup. Ct.



692; 48 Law. Ed. 1067. Justice Holmes stated (at page 454 of 194 U.S.):

“It is true that this general proposition is qualified by the fact that the ordinary limitations of actions are treated as laws of procedure, and as belonging to the *lex fori*, as affecting the remedy only, and not the right. But in cases where it has been possible to escape from that qualification by a reasonable distinction, courts have been willing to treat limitations of time as standing like other limitations, and cutting down the defendant’s liability wherever he is sued. The common case is where a statute creates a new liability, and in the same section or in the same act limits the time within which it can be enforced, whether using words of condition or not. *The Harrisburg*, 119 U.S. 199, 30 L.Ed. 358, 7 Sup. Ct. Rep. 140. *But the fact that the limitation is contained in the same section or the same statute is material only as bearing on construction.*\* It is merely a ground for saying that the limitation goes to the right created, and accompanies the obligation everywhere. *The same conclusion would be reached if the limitation was in a different statute, provided it was directed to the newly created liability so specifically as to warrant saying that it qualified the right.*”

This test has been uniformly adhered to. And in recent years Federal courts have in fact liberalized its application in order to find that the time limitation supplied by the law of the state where death occurred accompanies the right into jurisdictions where shorter limitations exist.

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\*Emphasis supplied throughout unless otherwise stated.

In *Theroux v. Northern Pac. R. Co.* (1894) 64 Fed. 84, the court, in considering this question, stated (at page 86 of 64 Fed.):

“It must be accepted, therefore, as the established doctrine, that where a statute confers a new right, which by the term of the act is enforceable by suit only within a given period, *the period allowed for its enforcement is a constituent part of the liability intended to be created, and of the right intended to be conferred.* The period prescribed for bringing suit in such cases is not like an ordinary statute of limitations, which merely affects the remedy.”

In *Boyd v. Clark* (1881) 8 Fed. 849, the court stated (at page 852 of 8 Fed.):

“The true rule I conceive to be this: That where a statute gives a right of action unknown to the common law, and, *either in a proviso to the section conferring the right or in a separate section, limits the time within which an action shall be brought, such limitation is operative in any other jurisdiction wherein the plaintiff may sue.*”

Although the rule of the earlier cases is clearly sufficient to compel a decision that the Nevada limitation is substantive in nature, later cases make such a result inescapable. The question herein involved was considered in *Maki v. George R. Cooke Co.* (1942) 124 Fed.2d 663. The court stated at page 666 of 124 Fed.2d):

“We see no valid reason why, if a state creates a statute a right non-existent at common law and prescribes in the same statute a limitation period for action which by comity will be applied in the forum of a sister state, *a limitation, though found in a separate statute of the creative state made applicable in express terms to actions commenced upon a liability*

*created by statute, should not likewise be recognized and applied in the courts of the forum state."*

The court concluded (at page 666 of 124 Fed.2d):

*"Nowhere else in the Minnesota Statutes is a limitation placed upon the right of action created by the ventilation statute of Minnesota, Section 4174. Why should not this limitation accompany the new right created by the statute wherever enforcement of the right is sought, if the substantive law of a sister state is, by comity, to be recognized and enforced?"*

*"To deny the just compulsion of this rhetorical question would be to whittle with a dull blade upon illogical niceties."*

It should be noted that the Minnesota statute was a general one, referring broadly, inter alia, to all actions commenced "*\* \* \** upon a liability created by statute, other than those arising upon a penalty or forfeiture." The court further stated:

*"The limitation of the Minnesota Statute, Sec. 9191, Mason's Minnesota Statutes of 1927, seems directed specifically enough to qualify the statutory liability created by the Minnesota Statute, embraced in Section 4174, idem.*

*"Section 9191 provides: 'The following actions shall be commenced within six years: 1. Upon a contract or other obligation, express or implied, as to which no other limitation is expressly prescribed. 2. Upon a liability created by statute, other than those arising upon a penalty or forfeiture. \* \* \*'"*

Aside from later liberal decisions, as represented by the *Maki* case, it is apparent from a consideration of the older cases above set forth that in two situations the

Federal courts will hold a time limitation on a cause of action for wrongful death to be substantive in nature. These situations are as follows: (1) Where the limitation is contained in a proviso to the cause of action, and (2) Where the limitation is contained in a different section of the same statute, but is directed specifically to the cause of action for wrongful death.

In *Calvin v. West Coast Power Co.* (1942) 44 Fed. Supp. 783, the court considered a State of Washington statute which enacted both the cause of action for wrongful death and a time limitation thereon into the Code of Civil Procedure of that State. The limitation, which did not even mention actions for wrongful death, was found in a separate chapter and title of the Code from the section creating the cause of action, and was classified generally with all other limitations on actions in the State of Washington in Title 2, Chapter 3 of *Remington's Revised Statutes of Washington*, entitled "Procedure in Courts of Record." The structure of Chapter 3 is as follows:

## "CHAPTER 3

### LIMITATION OF ACTIONS

§ 155. *Limitations prescribed — Objections, how taken.* Actions can only be commenced within the periods herein prescribed after the cause of action shall have accrued, except when in special cases a different limitation is prescribed by statute; but the objection that the action was not commenced within the time limited can only be taken by answer or demurrer.

§ 156. *Actions to be commenced in ten years.*  
(Setting forth various actions)



- § 157. *Within six years*  
(Setting forth various actions)
- § 158. *Within five years*  
(Setting forth various actions)
- § 159. *Within three years.*

Within three years:

2. An action for taking, detaining, or injuring personal property, including an action for the specific recovery thereof, or for any other injury to the person or rights of another not hereinafter enumerated;"

Section 159, Chapter 3, Title 2 of *Remington's Revised Statutes of Washington* embodies seven subdivisions which are directed to various types of actions. Subdivision 2 sets the time limitation on actions for wrongful death (*Robinson v. Baltimore & Seattle, M. R. Co.* (1901) 26 Wash. 484; 67 Pac. 274; *Dodson v. Continental Can Co.* (1930) 159 Wash. 589; 294 Pac. 265).

The court in the *Calvin* case held that this limitation was substantive in nature and inherent in the action for wrongful death when brought in the United States District Court in Oregon, and was controlling there, despite the fact that Oregon statutes provided a shorter limitation on actions for wrongful death. The court stated (at page 790 of 44 Fed. Supp. 789):

"The three-year limitation of the Washington law was incorporated in the Civil Code of that State, together with the statute permitting action for wrongful death, and thus, these sections may be considered part of the same enactment."



An application of the principles above set out demonstrates that the Nevada statute of limitations on actions for wrongful death is substantive in nature, and should follow the action in the instant case when filed in California. There is no Nevada decision construing this limitation as either substantive in nature or procedural in nature, and this Court is therefore free to decide the question for itself.

A consideration of the history of the Nevada limitation upon wrongful death actions shows that *this limitation and the cause of action for wrongful death created by Nevada law are part of the same statute*. In 1911 the Legislature of Nevada enacted an act entitled "*An Act to Regulate Proceedings in Civil Cases in This State and to Repeal All Other Acts in Relation Thereto*." This Act has been generally denominated the "Civil Practice Act." The cause of action for wrongful death was created by Chapter 69 of the said Act (Sections 9194 and 9195, Nevada Compiled Laws). The time limitation of two years on actions for wrongful death was set by Chapter 4 of the same Act (Section 8524, Nevada Compiled Laws). Chapter 4, Section 25, of the said Act states:

"Actions other than those for the recovery of real property, can only be commenced as follows:

"Within two years: (5) An action to recover damages for the death of one caused by the wrongful act or neglect of another."

The Nevada Legislature set forth this limitation in a separate section within Chapter 4 of the said Act and excluded all other actions from the limitation of this particular section. The Nevada Legislature could not have

used clearer means to direct this limitation specifically to the action for wrongful death alone, and no other. The time limitation here involved is much more specifically directed to the action for wrongful death than the limitation in the *Calvin* case, and of course, is more specifically directed to this one cause of action than the limitation considered in the *Maki* case. The Nevada time limitation of two years is therefore a substantive part of the cause of action rather than a matter of procedural law only.

**B. Since the Death of Appellant's Husband Occurred in the State of Nevada, the Nevada Statute of Limitations Is Applicable When a Suit for Wrongful Death Is Filed in California, Despite the Fact That Section 340(3) of the California Code of Civil Procedure Would Bar the Suit Had the Death Occurred in the State of California.**

There are no California decisions on this exact question, and this court is therefore free to decide the matter for itself. Section 340(3) of the California Code of Civil Procedure states:

§ 340. "*Within one year.* Within one year: 3. An action for libel, slander, assault, battery, false imprisonment, seduction of a person below the age of legal consent, *or for injury to or for the death of one caused by the wrongful act or neglect of another,* or by a depositor against a bank for the payment of a forged or raised check, or a check that bears a forged or unauthorized indorsement;"

It is apparent from reading this section that it does not purport to control or limit rights arising under the laws of another state. To construe the section as limiting such

rights, is to place upon it a strained and unnatural construction, and to impair the rights granted to appellant under the laws of the State of Nevada.

In *Theroux v. Northern Pac. R. Co.* (1894) 64 Fed. 84, the court passed on the exact point here involved, and stated (at page 85 of 64 Fed.):

“It follows, of course, that, if the courts of another state refuse to permit the cause of action to be sued upon during a part of the period limited by the foreign law, *to that extent they refuse to give effect to the foreign law, and by so doing impair the right intended to be created.* Doubtless, the courts of a state may refuse to enforce a liability unknown to the common law that has been created by the laws of a foreign state or country, but the rule of comity which prevails as between the various states of this Union requires that the courts of each state shall enforce every civil liability that may have been created by the laws of other states, for an act done or omitted within their several territorial jurisdictions, unless the liability so created and sought to be enforced is clearly repugnant to some local law, or is opposed to some well-established public policy of the state whose courts are asked to enforce it. \* \* \* Such being the rule of comity which is generally recognized and enforced, we do not see how the courts of Minnesota, *and much less a federal court sitting in Minnesota,* can well refuse to enforce a liability created by the laws of Montana for a wrongful act or omission of duty resulting in death, which was committed in Montana within three years, and more than two years prior to the institution of the suit, merely because the laws of Minnesota provide, with respect to similar acts committed in Minnesota, that suit shall be

brought within two years. *To refuse to entertain such a suit within three years would be to subtract from the liability, and to impair the right intended to be conferred by the laws of Montana;*”

In *Keep v. National Tube Co.* (1907) 154 Fed. 121, the identical question here involved was again considered. The court stated (at page 124 of 154 Fed.):

“The defendant contends that no action can be maintained on the Minnesota statute in New Jersey after the expiration of the period of 12 months limited in the New Jersey statute. It is true that actions are barred not by the *lex loci*, but by the *lex fori*; but the limitation of time within which an action may be instituted under the Minnesota statute, or that within which it may be instituted under the New Jersey statute, is so connected with the right of action itself that it does not operate as a mere limitation of time within which the remedy may be prosecuted. A general statute of limitations curtails a pre-existent common-law right; but the right of action for damages resulting from death is unknown to the common law. It is a new right created by statute for a limited period. In Minnesota that right exists for 2 years; in New Jersey it exists for 12 months. *One who acquires such a right under the New Jersey statute, or under the Minnesota statute, may carry it with him into any jurisdiction where a substantially similar right has been created. Why should the time within which such a right may be enforced be curtailed in a jurisdiction different from that in which the right was created by any statute other than one which, like a general statute of limitations, operates on the remedy only?* The New Jersey statute does not limit the time within which an action may be instituted under the Min-



nesota statute, for the reason that the New Jersey statute creates no right of action in any case where death has resulted from a wrongful act done in another state.”

In *Calvin v. West Coast Power Co.* (1942) 44 Fed. Supp. 783, the court, in considering the identical question here involved, stated (at page 788 of 44 Fed. Supp.):

“This court must attempt to discover in this situation what the Supreme Court of Oregon would hold *when these exact facts are presented for decision*. No case has been called to the attention of this court where such facts have been ruled upon by any tribunal sitting in Oregon.”

The court concluded that the statute of limitations of the State of Washington which allowed a period of three years within which to bring suit for a wrongful death should be applied when suit was filed in the United States District Court in Oregon despite the fact that the shorter limitation prescribed by the State of Oregon had expired prior to the filing of the action. The closing remarks of the court are peculiarly applicable to the situation presented in this appeal. The court stated (at page 790 of 44 Fed. Supp.):

“It is probable the Supreme Court of Oregon which has indicated a tendency to practical justice will not deny one injured by the death of a principal in another state access to this court while the right of action is alive in the jurisdiction of its origin. *Especially is this true where residents of Oregon have prevented service by remaining out of Washington.*”

The identical question here presented was also considered in *Wilson v. Massengill* (1942) 124 Fed.2d 666.



The court applied the statute of limitations of the state where the death occurred despite the contention that the suit was barred by the statute of limitations of the state where the suit was filed. The court stated (at page 66 of 124 Fed.2d):

“In a case decided today, *Nick Maki v. George R. Cooke Company*, 6 Cir., 124 F.2d 663, this court approved, applied and extended the doctrine of *Theroux v. Northern Pac. R. Co.*, 8 Cir., 64 F. 84, that where, by statute, a state creates a cause of action for death by wrongful act and prescribes in the same statute a limitation period for action, such limitation will be applied in the forum of a sister state, even though the period of limitation for like actions in the latter state is shorter. We apply that principle here. We find no indication of a contrary view in the reported cases in Tennessee. Decision upon the point presented was pretermitted in *Parsons v. American Trust & Banking Co.*, 168 Tenn. 49, 58, 73 S.W.2d 698. We are, therefore, free to decide the issue before us upon our own juristic reasoning. This we have done.”

(Certiorari denied by the Supreme Court, 316 U.S. 686; 62 Supreme Court 1274; 86 L.Ed. 1758)

The latest case on this exact point is *Lewis v. Reconstruction Finance Corporation* (1949) 177 Fed.2d 654. The court sets forth the two opposing views on the problem here involved, and states (at page 655 of 177 Fed.2d):

“However, there is a line of opposing authority which takes the view that as to rights of action of a purely statutory nature, such as the so-called wrongful death statutes, the time thereby prescribed for filing suit operates as a limitation of the liability itself as

created by the statute, and not of the remedy alone. It is deemed to be a condition attached to the right to sue. As such, time has been made of the essence of the right, which is lost if the time is disregarded. *The liability and the remedy being created by the same statute, limitation of the remedy must be treated as limitation of the right.*

“In dealing with this conflict of authority, unaided by any decision of this court directly in point, we conclude that the limitation laid down by the law of the state where the fatal injuries occurred should govern, unless the public policy of the forum is clearly opposed. We think this view is better supported by reason and authority.

“The fact that the Nebraska law provides a longer period for filing suit than the District law does not, in our opinion, manifest any conflict in policy between the two jurisdictions. The purpose of both is to create a right of action within a limited period for death occasioned by negligence. It is immaterial that the time for bringing suit differs in the two statutes. The principle underlying both is the same. *Weaver v. Baltimore & O. Railroad Co.*, 1893, 21 D.C. 499, 503.”

**C. When the United States District Court Denied Appellant's Right to Proceed with Her Action for the Wrongful Death of Her Husband, It Committed Reversible Error.**

When the court below applied the one-year limitation on actions for wrongful death contained in the California Code of Civil Procedure 340(3) to appellant's claim for the death of her husband, it violated well established principles of comity, and proceeded directly contrary to the great weight of authority as established by Federal decisions. It is apparent from a study of the Federal deci-

sions on this issue that Federal courts, when free to do so, have unanimously preserved a plaintiff's substantive rights acquired under the laws of one state, when circumstances require that those rights be enforced in a sister state. To do otherwise is to subtract from and impair the validity and effect of the laws of the state in which those rights were acquired. This is particularly true in this case, as it was in the *Calvin* case, since appellee is not doing business in Nevada, and accordingly could not be sued there. Appellee should be required to defend the case on the merits, and, assuming appellant can prove her case, to compensate appellant for the gross injury she has sustained. To do otherwise is to allow a wrongdoer to evade, by a technicality, the responsibility for its neglect of duty. The Federal courts of this country have thoroughly rejected such a position, and have adopted the only stand which is consistent with substantial justice to all parties.

**D. Appellant's Third Claim for Her Own Personal Injuries, Being a Claim Arising Out of Appellee's Breach of Warranty, Is Controlled by California Code of Civil Procedure 339(1).**

Appellee's liability arises out of an absolute obligation imposed by law. Suits to enforce such a liability are excluded from the scope of California Code of Civil Procedure 340 which sets up the one-year statute of limitations in California. This obligation arises out of a sale of goods and is imposed by law regardless of fault or negligence on appellee's part. In *Vaccarezza v. Sanguinetti* (1945) 71 C.A.2d 687 (163 P.2d 470) the California court

considered the nature of the liability for breach of warranty and stated (at page 689 of 71 C.A.2d):

“The action is not based upon the negligence of defendants but upon breach of the implied warranty of fitness for the purpose for which purchased (Civ. Code, Sec. 1735). *The section imposes an absolute liability regardless of negligence.* (*Gindraux v. Maurice Mercantile Co.*, 4 Cal.2d 206, 47 P.2d 708; *Jensen v. Berris*, 31 Cal. App. 2d 537; 88 P.2d 220). The warranty applies to the sale of food-stuffs for human consumption, and runs with the goods to the ultimate consumer, there being no requirement of privity between the ultimate consumer and the manufacturer. (*Klein v. Duchess Sandwich Co., Ltd.*, 14 Cal.2d 272; 93 P.2d 799; *Dryden v. Continental Baking Co.*, 11 Cal.2d 33; 77 P.2d 833.)”

The same problem is considered in *Williston on Sales, Revised Edition*, Section 237. The author there states:

“The effect of an express warranty undoubtedly is to bind the seller absolutely for the existence of the warranted qualities. If an implied warranty is properly called a warranty, the consequences should be similar. *It should make no difference, therefore, whether the seller was guilty of any fault in the matter. Such is the well-settled law of England. And either because of the enactment of the Sales Act or because of an interpretation of the common law most jurisdictions in the United States follow the English rule.* \* \* \*

The provisions of the American statute are, so far as this point is concerned, identical in meaning with those of the English Act, *and it seems clear that where either statute provides for a warranty, it means*



*an absolute undertaking that the goods possess the warranted quality."*

The author further comments on this question in a footnote to Section 237, stating:

*"In Rodgers v. Niles, 11 Ohio St. 48 \* \* \* the court said: 'If the sellers have failed through defect of material procured by themselves, or of workmanship, their contract is broken, whether such defect be latent or visible, and however honest their intention may have been.' The same rule seems adopted in Leopold v. Van Kirk, 27 Wis. 152. Section 2651 of the Code of Georgia, and section 1771 of the Civil Code of California (now superseded by the Uniform Sales Act) also seem to impose an absolute liability on the seller irrespective of any fault on his part. (citing Mary Pickford Co. v. Bayly, 12 Cal.2nd 501; 86 P.2nd 102) Moreover, the greater number of cases where the seller is held liable as a warrantor with no allegation or proof of negligence necessarily involve the point."*

When Section 340(3), California Code of Civil Procedure is considered in this connection, it is evident that it was never intended to control the suit for breach of warranty. Section 340, California Code of Civil Procedure states:

*"Within one year:*

*"3. An action for libel, slander, assault, battery, false imprisonment, seduction of a person below the age of legal consent, or for injury to or for the death of one caused by the wrongful act or neglect of another, or by a depositor against a bank for the payment of a forged or raised check, or a check that bears a forged or unauthorized endorsement;"*



The meaning of the phrase "caused by the wrongful act or neglect of another" was considered in *Basler v. Sacramento Electric, Gas & Ry. Co.* (1913) 166 Cal. 33; 134 P. 993. The court laid heavy emphasis on the fact that the words were intended to cover those actions where the gravamen of the complaint was the negligence of defendant, and rejected the plaintiff's contention that the negligence of defendant railroad constituted a breach of its contract of carriage. The court stated (at page 36 of 166 Cal.):

"In *Webber v. Herkimer*, 109 N. Y. 313; 16 N. E. 358, the question presented was whether or not a statute of limitations limiting the time within which an action to recover damages for 'a personal injury resulting from negligence' was applicable to the pleading in that case. The court held that whether the action was in form one arising *ex contractu* or *ex delicto*, the liability was referable to the common carrier's negligence and came within the statute relating to the limitation upon actions to recover damages for personal injuries and not to that prescribing the time within which a litigant might sue for damages for breach of contract.

"It has been held that the word 'for' means 'by reason of', 'because of' and 'on account of', and that a statute prescribing a limitation on 'actions for injury to the person \* \* \* caused by negligence' should be interpreted to mean 'actions' 'by reason of' or 'because of' or 'on account of' injuries to the person caused by negligence.' *Sharkey v. Skilton*, 83 Conn. 503, (77 Atl. 950)."

It is clear, therefore, that since this phrase was intended to control those actions which are in essence based

upon the negligence of defendant, all actions which are not based on the negligence or fault of defendant were intended to be excluded. Statutes of limitations are to be strictly construed and to hold that California Code of Civil Procedure 340(3) bars appellant's claim based on breach of warranty would enlarge the scope of this section as limited by the California courts. (*Nelson v. Merced County* (1898), 122 Cal. 644; 55 P. 421; *Skidmore v. County of Alameda* (1939) 13 Cal.2d 534; 90 P.2d 577.)

On the other hand, California Code of Civil Procedure 339(1) is specifically designed to cover the type of action here presented. This section states:

“Within two years;

1. An action upon a contract, obligation or liability not founded upon an instrument in writing, other than that mentioned in subdivision two of section three hundred thirty-seven of this code;”

In discussing the scope of this section, 16 Cal. Juris., Section 26 states (at page 465):

“The word ‘liability’ as used in this section is the most comprehensive of the several terms employed and includes both of the others. It is synonymous with the word ‘responsibility’ and includes within its scope contracts, express and implied, *liabilities arising in tort*, and all liabilities connected with instruments in writing but which do not arise therefrom directly or immediately. The section is intended, it has been said, to include all actions at law, not specially mentioned in other portions of the statute. If there is a statute expressly providing the time within which suit may be brought upon the particular liability, this section has no application.”

This section of the California Code of Civil Procedure is considered by the courts of California as the "general" statute of limitations in this State, and a consideration of its history shows that at one time it covered all actions for personal injuries including those arising by reason of the negligence or fault of the defendant. In *Piller v. Southern Pac. R.R. Co.*, (1877) 52 Cal. 42 the court applied the two-year limitation of this section when plaintiff sued for personal injuries incurred by reason of the defendant's negligence. The California Supreme Court there stated (at page 44 of 52 Cal.):

"We are of the opinion that the two years' limitation found in the first clause of the first subdivision of sec. 339 is applicable to all actions at law not specifically mentioned in other portions of the statute."

In 1905 the legislature of California amended Sec. 340(3) of the California Code of Civil Procedure to add the words here under consideration, and the section thereafter read as follows:

"Section Three Hundred and Forty. Within one year.  
 "Three—An action for libel, slander, assault, battery, false imprisonment, seduction *or for injury to or for the death of one caused by the wrongful act or neglect of another* or by a depositor against a bank for the payment of a forged or raised check."

The general meaning of Sec. 339(1) of the Code of Civil Procedure remained unchanged, however, and still covered all suits on liabilities *not specifically provided for elsewhere*.

In *Lattin v. Gillette*, (1892) 95 Cal. 317; 30 P. 545, the effect of Sec. 339(1) of the California Code of Civil

Procedure was again considered. The Court stated (at page 318 of 95 Cal.):

“Section 339 of the Code of Civil Procedure provided that an action upon a ‘contract, obligation, or liability,’ not founded upon an instrument in writing, must be brought within two years after the cause of action shall have accrued. This provision was declared in *Piller v. Southern Pacific R.R. Co.*, 52 Cal. 44, to be ‘applicable to *all actions at law not specifically mentioned in other portions of the statute.*’ The word ‘liability’ is the most comprehensive of the several terms used in this section, and includes both of the others, inasmuch as it is the condition in which an individual is placed after a breach of his contract, *or a violation of any obligation resting upon him.* It is defined by Bouvier to be ‘responsibility; the state of one who is bound in law and justice to something which may be enforced by action. *This liability may arise from contracts, either express or implied, or in consequence of torts committed*’; and this definition was approved in *Wood v. Currey*, 57 Cal. 209.”

It is clear, therefore, that the Legislature of California did not intend to remove actions based on the defendant's breach of warranty from the scope of California Code of Civil Procedure 339(1) by its enactment of the words under discussion into California Code of Civil Procedure 340(3). If the Legislature had intended, by so doing to remove *all* suits for personal injuries from the scope of California Code of Civil Procedure 339(1), it would have done so with unmistakable clarity by omitting the qualifying words “caused by the wrongful act or neglect of another” from California Code of Civil Procedure 340(3). The addition of these qualifying words limits the type of



actions removed from the scope of the "general" statute of limitations of two years in California, and this limitation confines the cases so removed to those where a personal injury is incurred by reason of the negligence or fault of the defendant. A suit for injuries arising as the result of a breach of warranty is based solely upon an absolute liability imposed by law, and is not dependent upon proof of the defendant's fault or negligence. A suit for this type of liability is therefore within the scope of California Code of Civil Procedure 339(1) prescribing a two-year statute of limitations, inasmuch as there is no specific limitation provided elsewhere.

In suits for a breach of warranty, both express and implied, the California courts have uniformly applied the two-year statute. (*Sweet v. Watson's Nursery* (1937), 23 Cal. App. 2d 379; 73 P.2d 284; *Mary Pickford Co. v. Bayly Bros. Inc.* (1939), 12 Cal.2d 501; 86 P.2d 102; *Brackett v. Martens* (1906), 4 Cal. App. 249, 87 P. 410; *Ackerman v. A. Levy & J. Zentner Co.* (1935), 7 Cal. App. 2nd 23; 45 P. 2nd 386; *Southern Cal. Enterprises v. Walter & Co.* (1947), 78 Cal. App. 2nd 750; 178 P. 2nd 785; *Menke v. Rand Mining Co.* (1947), 81 Cal. App. 2nd 169; 183 P. 2nd 755.)

As a matter of policy, there is no reason to include suits for breach of warranty within the one year limitation. A defendant will not be prejudiced by lapse of time, since in any event a suit based on such a breach cannot be maintained unless the defendant is notified within a reasonable time following the injury that a breach has occurred causing injury. (California Civil Code, Sec. 1769; *North Alaska Salmon Co. v. Hobbs, Wall & Co.* (1911) 159 Cal. 380; 113 P. 870; 120 P. 27.)



On the other hand, in the situation presented by modern distribution methods in the sale of goods, the buyer who suffers damage by breach of warranty may require considerable time in order to pursue the corporate defendant into a jurisdiction where it can be found "doing business."

Particularly is this true when, as in this case, the buyer was rendered violently ill, and was in addition faced with the death of her husband, and the necessary troubles and time-consuming arrangements in connection with such sickness and death (Tr. of Rec. 7).

It is respectfully submitted, therefore, that the court below erred in dismissing appellant's claim for her own personal injuries. As in the case of appellant's separate and distinct claim for damages incurred by reason of her husband's death, the appellee should be ordered to stand trial on the merits for the damages incurred by appellant personally.

Dated: San Francisco, Calif.,  
April 10, 1950.

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No. 12,477

IN THE

United States Court of Appeals  
For the Ninth Circuit

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MARY ZELLMER, as Administratrix of  
the Estate of Orval Zellmer, and  
MARY ZELLMER, an Individual,

*Appellant,*

VS.

ACME BREWING Co. (a corporation),

*Appellee.*

BRIEF FOR APPELLEE.

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No. 12,477

IN THE

**United States Court of Appeals  
For the Ninth Circuit**

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MARY ZELLMER, as Administratrix of  
the Estate of Orval Zellmer, and  
MARY ZELLMER, an Individual,

*Appellant,*

VS.

ACME BREWING CO. (a corporation),

*Appellee.*

**BRIEF FOR APPELLEE.**

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**STATEMENT OF THE CASE.**

The complaint in this case seeks a recovery for the alleged wrongful death of Orval Zellmer, and for personal injuries to Mary Zellmer all occurring in Nevada, and allegedly resulting from the negligent manufacturing or packaging of beer by defendant. The complaint shows on its face that both of these claims are barred if the California one year statute of limitations (C.C.P., § 340) is applicable. The District Court concluded that the California statute of limitations applied and dismissed the complaint.

This appeal presents clear and rather simple issues. There are, to begin with, a number of relevant rules of law which cannot be challenged. We are confident that appellant will not dispute the following:

1. This Honorable Court must apply and follow the California rules of conflict of laws.

*Griffin v. McCoach*, 313 U.S. 498, 61 S. Ct. 1023, 85 L. ed. 1481.

2. In all cases of conflict of laws, the *lex loci* governs only matters of substance, and all matters of procedure are governed by the law of the forum.

3. It is a universally accepted general rule that statutes of limitation are *procedural*, and that the limitation period of the law of the forum (California, in this case) is applicable. If the action is barred by the *lex fori*, it may not there be prosecuted even though the limitations period of the *lex loci* may not have run.

*Beale, Conflict of Laws*, page 1620;

*Crecich v. Giardino*, 37 C.A. (2d) 394 (99 P. (2d) 573).

We come now to the fourth rule; the application and extent of which is the basic issue on this appeal.

4. Where an action is created by statute (e.g., one for wrongful death) and, as a part thereof, the right so created is conditioned by a time limitation, such time limitation<sup>1</sup> is substantive and bars the right itself,

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<sup>1</sup>A time limitation of this kind is not a "statute of limitations" at all. *Adams v. Albany* (D.C., Cal., 1948), 80 F. S. 876. It is be-



rather than merely the remedy, with the result that when such time has elapsed, the *cause of action* is *extinguished*, and cannot (as can actions subject to procedural time limitations) be sued upon in other jurisdictions having longer procedural statutes of limitations.

*Davis v. Mills*, 194 U.S. 451, 24 S.Ct. 692, 48 L. ed. 1067.

In her first point on appeal, appellant attempts to extend the fourth rule above mentioned as follows: Appellant argues that such a substantive time limitation *must* govern the laws of *any* jurisdiction, and has the extraterritorial effect of compelling foreign Courts to entertain actions which, under the *procedural* laws of those jurisdictions would otherwise be barred. With this, we disagree. In answering appellant's first point, however, we will first assume that this extreme theory is correct, and show that appellant nevertheless cannot recover because the Nevada time limitation is *not* substantive; it is a typical, procedural statute of limitations. (Even appellant admits that if this is so, her action was properly dismissed.) We will then go further, however, and show as a second, independent answer that there can be no such legal doctrine as appellant relies on, and that, therefore, she cannot recover whether the Nevada limita-

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cause it is sometimes considered as such that confusion has arisen in some of the cases pertinent to this point. The two time elements relate to separate and different phases of conflict of laws: one, whether a cause of action exists (which is purely substantive), and two, whether such action, *if* it exists, may be prosecuted, as a procedural matter, in the court of the forum.

tion is procedural *or* substantive; that in either event the California statute of limitations must be applied.

Appellant's second point is that her action for her own personal injuries should not have been dismissed. Admittedly, California law governs here, and one of the sections of the California statute of limitations is to be applied. Appellant claims that she is suing for breach of warranty and that, therefore, the two year time limitation (C.C.P., § 339) applies rather than the one year limitation of C.C.P. § 340. We will show that this argument has been resolved many times, in California and elsewhere, adversely to appellant.

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#### APPELLEE'S CONTENTIONS.

Appellee contends that:

1. The action for wrongful death was properly dismissed because:

(a) The Nevada time limitation applicable to wrongful death is a purely procedural statute of limitations; and, therefore, even if the rule stated by appellant were correct, she cannot recover; and

(b) Independently of the above, the California statute of limitations must be applied whether the Nevada time limitation is substantive or procedural.

2. An action for personal injuries, even though couched in terms of breach of warranty, is barred by the one year statute of limitations.

THE ACTION FOR WRONGFUL DEATH WAS  
PROPERLY DISMISSED.

**A. The Nevada time limitation for wrongful death is a purely procedural statute of limitations.**

Appellant says that there is case law establishing the following rule: Where a wrongful death statute contains a substantive limitation on the right to sue (as distinguished from the usual procedural limitation which goes only to the remedy) that limitation operates in all jurisdictions not only to *extinguish* the right by passage of time, but it has also the extraterritorial effect of superseding the procedural remedial statutes of limitations of the *lex fori*, and compels the Courts of all other states to entertain the action at any time within the time limitation of the *lex loci*.

We will show later that there is no rule of law having the effect claimed by appellant. However, for the purpose of the point here being discussed we will *assume* the stated rule to be correct, and show that nevertheless appellant cannot recover.

If the above rule is correct, appellant, to take advantage of it, must demonstrate that the Nevada time limitation on actions for wrongful death is a substantive *condition of the right*, and not an ordinary procedural statute of limitations. If it is the latter, appellant must concede that the action was properly dismissed.

The difference between a statute which contains a substantive time limitation, and a statute which is subject to an ordinary, procedural statute of limitations, is exemplified in *Gregory v. Southern Pacific*

*Co.* (C.C., Ore., 1907), 157 Fed. 113. The Court there considered the construction of a number of wrongful death statutes with respect to the point here involved. It was specifically concerned with the California statute. It held that where such a statute itself contains a proviso (as did the original California death statute), the proviso is a part, and a limitation of the right; but where the death statute is silent as to the time of bringing the action, and the only limitation is found in the general limitations statute, the time element is procedural only. The Court said (pp. 118-119):

“Now, to apply the doctrine as thus illustrated and firmly established to the case in hand, it is clear from the statute of California, first enacted with the limitation of the time for commencement of the action subjoined as a proviso, that the limitation constituted a condition attending the bringing of the action, and was designed as a part and parcel of the liability created, and could not have been considered apart from the act giving the right of action as a limitation statute simply. But must not a different intendment be ascribed to the statute in its present form? Section 377 standing alone, as it does, gives the right of action merely, without qualification or limitation.

“It is contained in title 3, while the regulation of the time for the commencement of actions in general is contained in the preceding title.

\* \* \* \* \*

“Thus it will appear that the statute of limitations is completely segregated from the statute giving the right of action. Furthermore, the limitation was formerly from the time of the death



of the party injured, while now it begins to run from the time the cause of action accrued; showing that, by a rearrangement of the statutes, and their adoption in that form, a different purpose was to be subserved, and we must ascribe to such statutes, therefore, another and different intendment. That intendment, manifestly, is to place the right of action accorded by section 377 in the category of other causes, and to apply the statute of limitations to that action in manner and substance as applied to all other civil actions, treating it as a part of the remedy only, and not as a condition to the cause."

See, also:

*Anderson v. Linton* (7th Cir., 1949), 178 F. (2d) 304;

*Hughes v. Lucker* (3rd Cir., 1949), 174 F. (2d) 285;

*Keys v. Pullman Co.* (D.C., Tex., 1949), 87 F. Supp. 763;

8 *Cal. Jur.* 1041-1042.

Under these authorities, the Nevada wrongful death statute is clearly procedural. The statute is, along with most other Nevada causes of action, a part of the Nevada "Civil Practice Act". There are three Nevada laws governing death actions. The first is contained in Chapter 6, § 55, of the Act, entitled "PARTIES", and provides (Nevada Compiled Laws, § 8554):

"When the death of a person not a minor is caused by the wrongful act or neglect of another, his heirs, or his personal representatives for the benefit of his heirs, may maintain an action for



damages against the person causing the death, or, if such person be employed by another person who is responsible for his conduct, then also against such other person. If such adult person have a guardian at the time of his death, only one action can be maintained for the injury to or death of such person, and such action may be brought by either the personal representatives of such adult person deceased for the benefit of his heirs, or by such guardian for the benefit of his heirs as provided in section 54. In every action under this and the preceding section such damages, pecuniary and exemplary, may be given as under all the circumstances of the case may be just. As amended, Stat. 1939, 17."

The second and third are contained in Chapter 68 of the Act, entitled "Death By Wrongful Act, Action For", §§ 705, 706, and provide (Nevada Compiled Laws, §§ 9194 and 9195):

"9194. Whenever the death of a person shall be caused by wrongful act, neglect or default, and the act, neglect or default is such as would, if death had not ensued, have entitled the party injured to maintain an action and recover damages in respect thereof then, and in every such case, the persons who, or the corporation which would have been liable if death had not ensued shall be liable to an action for damages notwithstanding the death of the person injured; and although the death shall have been caused under such circumstances as amount to a felony."

"9195. The proceeds of any judgment obtained in any action brought under the provisions of this chapter shall not be liable for any debt

of the deceased; provided, he or she shall have left a husband, wife, child, father, mother, brother, sister, or child or children of a deceased child; but shall be distributed as follows:

“If there be a surviving husband or wife, and no child, then to such husband or wife; if there be a surviving husband or wife, and a child or children, or grandchildren, then, equally to each, the grandchild or children taking by right of representation; if there be no husband or wife, but a child or children or grandchild or children, then to such child or children and grandchild or children by right of representation; if there be no child or grandchild, then to a surviving father or mother; if there be no father or mother, then to a surviving brother or sister, or brothers or sisters, if there be any; if there be none of the kindred hereinbefore named, the proceeds of such judgment shall be disposed of in the manner authorized by law for the disposition of the personal property of deceased persons; provided, every such action shall be brought by and in the name of the personal representative or representatives of such deceased person; and provided further, the court or jury, as the case may be, in every such action may give such damages, pecuniary and exemplary, as shall be deemed fair and just, and in so doing may take into consideration the pecuniary injury resulting from such death to the kindred as herein named. As amended, Stats. 1939, 17.”

None of these statutes *condition* the right therein granted by any substantive time limitation. As is the case in California (see C.C.P. § 377), the right is

simply granted without qualification, substantive or otherwise, as to time.

The general provisions of Nevada law governing commencement of all civil actions is contained in Chapters 1, 2, 3 and 4 of the Practice Act. Chapter 4 is entitled "Limitations other than Real Property", and Section 25 provides (Nevada Compiled Laws, sec. 8524) :

"Section 25. Actions other than those for the recovery of real property, can only be commenced as follows:

"*Within six years:* \* \* \*

"*Within four years:* \* \* \*

"*Within three years:* \* \* \*

"*Within two years:* 1. An action against a sheriff, coroner, or constable, upon the liability incurred by the doing of an act in his official capacity and in virtue of his office, or by the omission of an official duty, including the nonpayment of money collected upon an execution.

2. An action upon a statute for a penalty or forfeiture, where the action is given to an individual, or to the state, or an individual and the state, except when the state imposing it prescribes a different limitation.

3. An action for libel, slander, assault, battery, false imprisonment or seduction.

4. An action against a sheriff, or other officer, for the escape of a prisoner arrested or imprisoned on civil process.

5. *An action to recover damages for the death of one caused by the wrongful action or neglect of another.*

“*Within one year: \* \* \**” (Emphasis supplied.)

It is clear that the time element applicable in Nevada to the Nevada wrongful death actions is nothing more or less than a procedural statute of limitations. There is no basis whatever upon which it can reasonably be said to differ from the other limitations periods among which it is placed, and no basis upon which it can be said to qualify the *right* as distinguished from the remedy for wrongful death.

The Nevada statutes are practically identical with the California statutes on the same point. The California wrongful death statute, it has been established, contains no substantive time limitation. It is subject to an ordinary, procedural statute of limitations.

*Gregory v. Southern Pacific Co.*, supra.

Appellant urges that “A consideration of the history of the Nevada limitation upon wrongful death actions shows that *this limitation and the cause of action for wrongful death created by Nevada law are part of the same statute.*”<sup>1a</sup> This argument alone demonstrates the weakness of appellant’s position. The “same statute” referred to is the Nevada “Civil Practice Act”. This Act is actually a combined Civil Code and Code of Civil Procedure. It contains not only the wrongful death statute of limitations, but *all* limitations provision, of Nevada Civil Law; it contains not

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<sup>1a</sup>Appellant’s Op. Br., p. 12.



only the law governing wrongful death, but the law of negligence, libel, slander, etc., as well. It even contains the Nevada statutes establishing and regulating the State Justices' Courts.

If appellant's argument were at all sound, it would necessarily follow that *all* of the limitations periods of the Act were substantive, since they are in the "same Act" as the actions to which they refer.

The same argument was before the Court in *Gregory v. Southern Pacific Co.*, supra, for in California, both the wrongful death statute and the one year statute of limitations are contained in the Code of Civil Procedure, which, of course, is "one act".<sup>2</sup>

It is probably a fact that most wrongful death statutes do contain within themselves, substantive time limitations. See, for example, the statutes discussed in *Gregory v. Southern Pacific Co.*, supra, and those involved in the cases cited in appellant's brief.

California and Nevada, however, have chosen *not* to so limit the right which they have granted.

Appellant seeks in her brief to convey the impression that statutes which have substantive time limitations are more liberal, equitable or just than those which are subject to procedural statutes of limitations. Exactly the contrary is true.

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<sup>2</sup>The California "Act" is entitled: "An Act to establish a Code of Civil Procedure", approved March 11, 1872, and section 1 of the C.C.P. states: "This Act shall be known as The Code of Civil Procedure of California \* \* \*."



A substantive time limitation *destroys without qualification* the cause of action itself not only in the *lex loci*, but in all other jurisdictions. Where, on the other hand, the limitation is procedural, the running of time does *not* extinguish the right, but merely bars the remedy. Therefore, suit can be brought upon the cause of action which, of course, continues to exist, in any jurisdiction, the statute of which has not run, even though the remedy is barred in the *lex loci*.

*Keys v. Pullman Co.* (D.C. Tex., 1949), 87 F. Supp. 763.

Further, if the limitation is substantive it cannot be waived; nor can it be tolled by fraud, concealment, absence from the state, insanity, or for any other reason. If substantive, the mere passage of time irrevocably and completely destroys the cause of action.

*Midstate Horticultural Co. v. Penna. Ry. Co.*,  
321 U.S. 356, 64 S. Ct. 128, 88 L. ed. 96;

*Ewing v. Risher* (10 Cir., 1949), 176 F. (2d)  
641;

*Adams v. Albany* (D.C., Cal., 1948), 80 F.  
Supp. 876;

*Partee v. St. Louis & S.F. Ry.* (8th Cir., 1913),  
204 Fed. 970;

*Mullins v. DeSoto Securities Co.* (D.C., La.,  
1944), 56 F. Supp. 907 (Aff'd, 149 F. (2d)  
864);

*Wilson v. Missouri Pac. Ry. Co.* (D.C., Ark.,  
1945), 58 F. Supp. 844.

See many other cases in 132 A.L.R. 292.

It is clear that a substantive time limitation on the right (rather than on the remedy) is a very real, and normally harsh limitation. The more liberal statutes do not so limit the cause of action so created.

Finally, it is established that this Honorable Court must apply to this case the same rule of conflict of laws which a California Court would apply.

*Kaxon Co. v. Stentor Electric Mfg. Co.*, 313

U.S. 487, 61 S. Ct. 1020, 85 L. ed. 1477;

*Keys v. Pullman Co.* (D.C., Tex., 1949), 87 F. Supp. 763;

*Griffin v. McCoach*, 313 U.S. 498, 61 S. Ct. 1023, 85 L. ed. 1481.

Since the California statute is procedural, and since the Nevada statute is practically identical to it, it seems self-evident that California would hold that the Nevada time limitation is procedural, not substantive. Such a holding, even under the theory of law argued by appellant, disposes of this appeal.

In any event, however, in the case of *Engel v. Davenport*, 194 Cal. 344 (228 P. 710), the California Supreme Court adopted a rule of conflict of laws which is conclusive of the issues on this appeal. In that case the Court followed what we will later show to be the proper rule, and held that the California statute of limitations is applicable to *all* suits brought within its jurisdiction, whether or not such suits were created by foreign statutes, and whether or not such foreign statutes contained substantive time limitations. The case involved an action under the United States

Merchant Marine Act, which contained a substantive two year time limitation. The Court applied the California one year statute, saying (pp. 351-352):

“It is true that there is an exception to the general rule that the law of the forum controls to the effect that when a statute which creates a new liability limits the time within which the right may be enforced, an action seeking to enforce such right can be maintained only within the time limited by the statute creating the right, regardless of the jurisdiction in which the action was instituted. (*Davis v. Mills*, 194 U.S. 451, 454 (48 L. Ed. 1067, 24 Sup. Ct. Rep. 692); *The Harrisburg*, 119 U.S. 199, 214 (30 L. Ed. 358, 7 Sup. Ct. Rep. 140, see, also, Rose’s U. S. Notes); *Vaught v. Virginia & Southwestern R. R.*, 132 Tenn. 679 (179 S.W. 314).) Such exception to the general rule is not, in our opinion, applicable to the instant case.

“The exception to the general rule that the law of the forum governs is based upon the reasoning that when the liability and the remedy are created by the same statute, time is made of the essence of the right, and when the time prescribed by the statute has expired, the cause of action itself is extinguished. The lapse of time prescribed by the statute creating the new right having operated to extinguish the right, no right remains thereafter to support the action and consequently no action can be thereafter maintained in *any* jurisdiction. Obviously this reasoning applies only when the period prescribed by the statute creating the liability is *shorter* than the period provided by the law of the forum. There is no logical reason why the doctrine that the

limitation prescribed by the statute of another jurisdiction, which creates a right of action, is a condition of the right of action so that the latter is extinguished when the time so prescribed has expired, and will not thereafter sustain an action anywhere should exclude the operation of the general rule which refers the question of limitation to the law of the forum, if the period prescribed by the statute of the other jurisdiction creating the liability has not expired. (46 L.R.A. (N.S.) 687.) The exception to the general rule being based upon the theory of the extinguishment of a right by the lapse of time, if the time prescribed by the statute creating the right is *longer* than the time provided by the law of the forum, such actions will not fall within the exception but will be governed by the general rule that the law of the forum—in the instant case, the state statute of limitations—will prevail. (*Weaver v. Baltimore & O. R. Co.*, 21 D.C. (10 Mackey) 499; *Hutchings v. Lamson*, 96 Fed. 720 (37 C.C.A. 564); 2 Wharton on Conflict of Laws, 3d ed., sec. 540b, pp. 1264, 1265.)” (Emphasis supplied.)

This case establishes the California law, and is a conclusive answer to appellant's contention.<sup>3</sup>

With one exception, all of the decisions relied upon and cited by appellant involve statutes where the time

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<sup>3</sup>The result of this case was reversed in 271 U.S. 33, 70 L. ed. 813, on the ground that this was not a case involving conflict of laws. Since the act involved was a federal law, it could not conflict with state law because acts of Congress are the supreme law of the land, and the provisions of federal law stated by Congress “in the exercise of its *paramount authority*” must control. The case does, of course, state the California rule applicable to conflicting *state* laws, over which rule the U.S. Supreme Court has no authority.



limitation is clearly a substantive limitation on the right, and, therefore, are not in point. The one exception is the case of *Maki v. George R. Cooke Co.* (6 Cir., 1942), 124 F. (2d) 663, decided on the same day, and by the same Court that decided *Wilson v. Massengill* (6 Cir., 1942), 124 F. (2d) 666.

That Court held what appeared to be a procedural statute, to be substantive. We believe that the Court's error was based upon its failure to realize that the distinction is more than a mere isolated technicality. As we have shown above, serious, restrictive consequences flow from a holding that a time limitation is substantive. The Court in the *Maki* case failed to perceive this, and thought that the distinction involved "whittling with a dull blade upon illogical niceties" The decision does not, however, coincide with the law of California, which is clearly laid down in *Engel v. Davenport*, *supra*.

There are two cases cited by appellant which deserve some comment. They are *Calvin v. Western Coast Power Co.* (D.C., Ore., 1942), 44 F. Supp. 783, and *Lewis v. R.F.C.* (D.C., Ct. App., 1949), 177 F. (2d) 654. In those cases, the time limitation of the statute of the *forum* was a substantive part of the *forum's* wrongful death statute. The *lex fori*, therefore, had *no* procedural statute of limitations applicable generally to death actions. Obviously, a substantive part of the *forum's* statute could not be invoked to bar, procedurally, a cause of action based on a different statute. (Here again, note the differ-



ence in *essence*, between a condition on the right, and a statute of limitations.) There was, therefore, in those cases, no statute of limitations at all in the *lex fori* which would bar the actions sued upon. Appellant relies upon these cases in making the brief contention that the California statute of limitations does not purport to apply to any but California death actions. Our statute is *procedural*, not substantive. It applies to *all* actions for wrongful death. It states (C.C.P., 340): "Within one year: \* \* \* an action for injury to or for the death of one caused by the wrongful act \* \* \*" If appellant's argument were correct it would have to apply to foreign actions for personal injuries also, which is manifestly ridiculous.

We say, therefore, that even if there is a rule of law such as stated by appellant, it cannot apply to this case because (1) the Nevada time limitation is a procedural statute of limitations, and not a substantive condition of and limitation on the right itself, and (2) California does not recognize any such rule and has decided that its procedural statutes of limitations apply to bar actions of all kinds.

**B. The California statute of limitations applies to this action whether the Nevada time limitation is substantive or procedural.**

We believe that the point just discussed adequately answers appellant's contention. However, that discussion was based upon the assumed existence of a rule which actually does not exist. It is only because a few cases have misconceived and misapplied cer-

tain basic principles of conflict of laws that any such argument is possible at all. Except for such cases, it is established by principle and authority that the statute of limitations of the forum is always available as a bar to the remedy, whether the foreign statute contains a substantive or procedural time limitation.

At the outset, the two different fact situations must be kept in mind: (1) Where, under the *lex loci*, the time to sue has expired, but the time has not expired under the statutes of the forum; and (2) where the time to sue has not expired under the *lex loci*, but has expired under the laws of the *lex fori*.

In the first situation, if the time limitation of the foreign statute is *procedural*, the right remains alive and may be prosecuted in any state in which the limitations period has not run. This is true even though suit could no longer be brought in the *lex loci*. *Keyes v. Pullman Co.*, supra. If, however, the time limitation is *substantive*, the action may not be brought anywhere, for the expiration of time extinguishes the right as well as the remedy. There are no conflicting cases on this point.

In the second fact situation, if the time limitation is *procedural*, the law of the forum clearly applies.

There is no conflict on this point. The following discussion is concerned solely with the second fact situation, when the *lex loci* time limitation is *substantive*, for it is in this area that some cases have created some confusion.

Actually, there is only one broad consequence of a substantive time limitation. It irrevocably and unqualifiedly limits the time within which suit may be brought *anywhere in the world*, and withdraws all alleviating circumstances, such as waiver, fraud, etc., to which statutes of limitation are subject. That is the specific, express purpose of a statute which conditions the *right* upon bringing suit within a given time. Such a condition, of course, operates substantively, for, by its express terms, it extinguishes the cause of action by lapse of time. The result is that a *cause of action* cannot be stated.

Such a substantive limitation cannot, however, have the effect of repealing or nullifying the *procedural* laws of another state. (See 11 *Am. Jur.*, 310, 311.) Those procedural laws are to be applied in these cases as in all others. The substantive law of the *lex loci* determines whether a cause of action exists. Once that is determined, the *lex loci* becomes unimportant. The question of whether the right may be enforced, procedurally, depends upon the *lex fori*, including its applicable statutes of limitations.

Applying these principles to the case at bar, whether a cause of action *exists* is determined by the *lex loci*. This is a substantive question over which the *lex fori* can have no control. In determining whether such a cause of action exists, a substantive time limitation in the foreign statute is important, since it does operate substantively; if the time has not elapsed, a cause of action can be stated. If the

time has elapsed, the cause of action is extinguished, and suit cannot be brought on it in the forum or anywhere else in the world. Once this question is determined, the application of the substantive law of the foreign state, including the time condition, is at an end.

If the plaintiff can bring herself within the foreign statute, a cause of action is stated, and from that time on, all procedural matters, including the question of whether the forum will entertain this admittedly existing cause of action under its procedural statute of limitations, are governed by the *lex fori*. In other words, the statute of limitations of the forum operates procedurally, in a completely different field. It, unlike the substantive limitation, may be waived if not pleaded as a defense; it may be tolled, there may be an estoppel. All of these matters are procedural, and are matters of the *lex fori* over which the foreign state has no control. These procedural statutes have nothing to do with substantive time conditions on rights. A foreign state could not nullify such procedural laws of the forum even if it tried.

That this is the rule in California is clear from the above quotation from *Engel v. Davenport* (supra, pp. 15, 16). See also, *Hospelhorn v. Van Dusen*, 40 C. A. (2d) 257 (104 P. (2d) 888), and 8 *Cal. Jur.* 1041, 1042.

That it is the only true, logical rule is established by the following authorities:

68 A. L. R. 217;



*Hutchings v. Lamson* (7 Cir., 1899), 96 Fed. 720;

*Hughes v. Lucker* (3 Cir., 1949), 174 Fed. (2d) 285;

*Restatement, Conflicts of Law*, § 397(b);

II *Wharton on Conflict of Laws* (3rd ed., Parmele), 1264, 1266;

3 *Beale, Conflict of Laws*, 1627-1629.

In the annotation referred to, the author states:

“In accordance with the fundamental principle of law that matters pertaining to the remedy are governed by the law of the state or country where suit is brought, rather than that in which the cause of action arose, it is well settled that the statute of limitations of the country, or state, where the action is brought and the remedy is sought to be enforced, controls, in the event of the conflict of laws. In other words, the *lex fori* determines the time within which a cause of action may be enforced. 17 R.C.L. pp. 697 and 698:

“However, where the foreign statute creating a cause of action not known to the common law prescribes a *shorter* period in which action may be commenced than that prescribed by the law of the place where the action is brought, the former, the *lex loci*, governs, and no action can be maintained in any jurisdiction, foreign or domestic, after the expiration of such period, since the limitation is, in such a case, a qualification or condition upon the cause of action itself, imposed by the power creating the right, and not only is action barred, but the cause of action itself is extinguished, upon the expiration of the limitation period. Parmele’s *Wharton, Conf. L.* § 540b.



“It by no means follows, however, that the limitation of the forum would not apply as a bar to the action, where such limitation is shorter than that prescribed by the *lex loci*. As demonstrated by the editor of Parmele’s Wharton, Conflict of Laws, § 540b, the reason why the lapse of time prescribed by the statute creating the cause of action precludes an action thereon in other jurisdictions is that it extinguishes the cause of action itself. The condition prescribed by the *lex loci* is not a statute of limitation at all, properly speaking; so, the application of the *lex loci* in such a case is not really in derogation of the general rule that, where there is a conflict between a statute of limitation of the forum and one of the place where the cause of action arose, the former governs. Where the *lex fori* prescribes a shorter period of limitation, there seems to be no reason for not giving effect thereto, in accordance with the general rule. In such a case, where the period fixed by the *lex loci* has not elapsed, the plaintiff has a concededly existing cause of action; *but it is to existing causes of action, and only to such* that statutes of limitations are intended to apply; and the limitation of the forum does no more in denying relief on a statutory cause of action, than in cutting off the remedy on an equally valid cause of action at common law.” (Emphasis supplied.)

In II *Wharton on the Conflict of Laws* (3rd ed., Parmele), at pages 1264 to 1266, the author states:

“While the bar of the statute by which the cause of action is created thus precludes the maintenance of an action thereon in another jurisdic-

tion, the law of which allows a longer period, the converse is not necessarily true; though some of the cases hold that the statute creating the cause of action governs in this respect, when it prescribes a shorter period than that fixed by the law of the forum. (*Citing Therox v. Northern P. Ry. Co.*, 64 Fed. 84.) This view, however, seems to rest upon a misapprehension. The reason the lapse of the time prescribed by the statute creating the cause of action prevents the maintenance of an action in another jurisdiction is that it extinguishes the cause of action, and there is thenceforth nothing to support an action in any jurisdiction. Assuming, however, that the time allowed by the foreign statute creating the cause of action has not expired, the plaintiff comes to the bar of the forum with a concededly existing cause of action; but it is not apparent why an action thereon does not, as in the case of an existing cause of action at common law, fall within the operation of the general principle that the limitation of actions is governed by the law of the forum. It may be that the same principle which characterizes the limitation prescribed by the foreign statute as a condition affecting the right of action itself, and not merely the remedy, will, when applied to the corresponding statute of the forum creating a similar cause of action, characterize the limitation prescribed by that statute as a matter of right rather than of remedy, and thus confine its operation to causes of action arising at the forum. This is by no means clear, however, since such a limitation appears to affect both the right and the remedy; and if it does affect the remedy it is applicable to foreign causes

of action not barred by the statute of their creation. But, even assuming that the special limitation prescribed at the forum affects the right only, and not the remedy, and is therefore not applicable to foreign causes of action, there may be a general limitation at the forum, which upon the general principle that limitation is governed by the law of the forum is applicable to foreign, as well as domestic, causes of action. If there is no general or special limitation at the forum applicable to foreign causes of action, the action may doubtless be entertained if the bar of the foreign statute has not fallen; but, upon the hypothesis assumed, this result is not due to the fact that the foreign limitation governs, but because it happens that there is no limitation at the forum applicable to the case."

In *Restatement, Conflicts of Law*, sec. 397(b), it is said:

"b. *Statute of limitations at forum.* The limit of time in the death statute of the forum may be interpreted as a statute of limitations for all actions for death irrespective of the place of wrong, as well as a statute limiting the existence of rights created by the statute (see §605); and in that case the suit must be brought within the time limited in that statute, as well as within the time limited in the statute of the place of injury."

In *Hutchings v. Lamson*, *supra*, an action was brought in Illinois to enforce a Kansas statute creating stockholders' liability. The Court said (p. 721):

"The contention of the plaintiff in error that the Kansas statute of limitations alone can have

any application to the case is manifestly not tenable. The general rule is that in respect to the limitations of actions the law of the forum governs, and while the courts will enforce a limitation established under the law of another state, when applicable, it does not do so to the exclusion of the law of the forum. It would involve serious and possibly absurd consequences, if it were established that a right of action created and governed by the law of Kansas could be enforced in Illinois after the time when, by the law of the latter state, the action had been barred. The cases cited show that the law of Kansas, if applicable, will be enforced in Illinois, but they do not say nor imply that a like or different limitation by the statute of Illinois may not apply."

The cases cited by appellant are, for the most part, consistent with, and a part of this correct rule.

In *Davis v. Mills*, 194 U.S. 451, 24 S. Ct. 692, 48 L. ed. 1067, and *Boyd v. Clark* (C.C., Mich., 1881), 8 Fed. 849, the Courts merely held that since the time limitations in the statutes involved were substantive, and that that time had elapsed, necessarily the action (not merely the remedy) was extinguished.

As already pointed out, the cases of *Calvin v. Western Coast Power Co.*, supra, *Lewis v. R.F.C.*, supra, and *Keep v. National Tube Co.* (C.C., N.J., 1907), 154 Fed. 121, involve situations where the time limitation of the law of the *forum* was a substantive part of the *forum's* wrongful death statute,



and could not, therefore, be given procedural application to *other* wrongful death statutes.

The cases of *Maki v. George R. Cooke Co.*, supra, *Wilson v. Massengill* (6 Cir., 1942), 124 F. (2d) 666, supra, and *Theroux v. Northern Pac. Ry. Co.* (8 Cir., 1894), 64 Fed. 84, are, we submit, wrong in principle and logically unsupportable. The *Maki* and *Wilson* cases were decided on the same day by the same Court, which Court so misconceived the subject matter of its decision that it likened the problem to whittling "away with a dull blade upon illogical niceties". The decision in the *Wilson* case contrasts unfavorably with a decision it overturned, *Cauley v. S. E. Massengill Co.* (D.C., Tenn., 1940), 35 F. Supp. 371.

In arguing that the procedural law of the forum applies whether or not Nevada's statute of limitations is substantive or procedural, we have undertaken a burden which we do not really have. We say this because the Nevada statute of limitations is so obviously procedural. We have lengthened this brief by discussing this second point in the hope that the decision of this Honorable Court will clarify the confusion evident in a few of the cases on the point.

**C. An action for personal injuries, even though couched in terms of breach of warranty, is barred by the one year statute of limitations.**

If the allegations of appellant's complaint are true, she suffered personal injuries as a result of the negligent manufacture or packaging of beer. She could,



therefore, state a cause of action irrespective of any breach of warranty.

*Dryden v. Continental Baking Co.*, 11 Cal. (2d) 33 (77 P. (2d) 833);

*Klein v. Duchess Sandwich Co.*, 14 Cal. (2d) 272 (93 P. (2d) 799).

In any event her action is one for "personal injuries" which is barred if not brought within one year. California Code of Civil Procedure, sec. 340. This section does not say that it relates only to "personal injuries" resulting from torts, but not from breaches of warranty. It relates to *all* actions for personal injuries.

Appellant's argument is ingenious, but it was made, and the answer settled, fifty years ago. The following cases are directly contrary to appellant's contention:

*Singley v. Bigelow*, 108 Cal. App. 436 (291 Pac. 899);

*Escola v. Coca-Cola Bottling Co.*, 24 Cal. (2d) 453 (150 Pac. (2d) 436);

*Automobile Ins. Co. v. Union Oil Co.*, 85 C. A. (2d) 302 (193 P. (2d) 48);

*Harding v. Liberty Hosp. Corp.*, 177 Cal. 520 (171 Pac. 98);

*Basler v. Sacramento Elec. Gas Ry. Co.*, 166 Cal. 33 (134 Pac. 993);

*Huntley v. Zurich Ins. Co.*, 100 C. A. 201 (280 P. 163);

*Rushing v. Pickwick Stage System*, 113 C. A. 240 (298 Pac. 150);

*Marty v. Somers*, 35 C. A. 182 (169 P. 411);

*De Mirjian v. Ideal Heating Corp.*, 91 C. A. (2d) 905 (206 P. (2d) 20).

In *Singley v. Bigelow*, *supra*, the Court said (pp. 438, 444-446):

“The complaint then states that on the twenty-first day of January, 1929, the plaintiff Nettie S. Singley requested one Harold Hopper to go to the drugstore of Justin O. Bigelow and purchase for her a certain amount of epsom salts and quinine, and for the purpose of having said Harold Hopper obtain said articles she wrote the names of the same upon a piece of paper and directed the said Harold Hopper to hand that paper to the person in charge of the drug-store belonging to the said Justin O. Bigelow; that at said time Frank Bigelow, hereinbefore mentioned, was in charge of said store, and gave to the said Harold Hopper the amount of said epsom salts requested, and also gave him a small box of powder labeled Quinine in the handwriting of said Bigelow. It further appears from the complaint that the box labeled ‘Quinine’ in fact contained mercury powder; that the plaintiff Nettie S. Singley took several doses of said powder, under the impression that she was taking quinine; that as a result of taking said mercury powder, said Nettie S. Singley became very ill, suffered a great deal of pain and many ills which we need not mention. \* \* \*

“The cause of action which we are considering is not one *ex contractu*. Paragraph X of the complaint which we have set forth bases the whole right of the plaintiffs to recover, upon the negli-

gence of the deceased. All the injuries therein mentioned are alleged to have arisen from, and flowed out of such negligence. It is purely an action of tort based upon the personal wrong suffered by reason of the action of the deceased, and not upon any breach of contract on his part. *The personal injuries constitute the gravamen of the charge.* Everything else is incidental. The distinction as to what constitutes a cause of action for injury to the person and an injury to property is clearly drawn in the case of *Wikstrom v. Yolo Fliers Club*, 206 Cal. 461 (274 Pac. 959). \* \* \*

“The implied warranty of a druggist as to the quality of the drugs sold does not change the action in the event of negligence. (19 C. J., p. 783.) It is there said: ‘An action against a druggist to recover for personal injuries should be ex delicto, not ex contractu. Every material fact which constitutes the ground of plaintiff’s cause of action must be stated, and where negligence is the basis for the action it must be alleged in plaintiff’s complaint. \* \* \* Where plaintiff charges both common law and statutory negligence and is not required to make an election, he may prove and recover on either.’ \* \* \*

“In *Marty v. Somers*, 35 Cal. App. 182 (169 Pac. 411) the cause of action was pleaded as arising ex delicto. The court said: ‘That even if we should regard it as arising upon contract, nevertheless, the damages sought are directly referable to the personal injuries suffered,’ etc. We think this case applies directly to the case at bar. \* \* \*

“In *Basler v. Sacramento Ry. Co.*, 166 Cal. 33 (134 Pac. 993), where the statute of limitations was involved, depending upon whether the action pleaded was one *ex contractu* or *ex delicto*, the holding of the court was that the gravamen of the charge rested upon the personal injuries inflicted, and was, therefore, *ex delicto*, and that the pleader having set forth a cause of action based upon a personal tort, it could not be upheld as an action *ex contractu*. Without quoting from the *Basler* case, it is sufficient to say that the rule announced in that case is controlling here. The case of *Basler v. Sacramento Ry. Co.*, *supra*, was followed and approved in *Harding v. Liberty Hospital Co.*, 177 Cal. 520 (171 Pac. 98), where a number of cases are cited to the same effect.”

In *Escola v. Coca-Cola Bottling Co.*, *supra*, a manufacturer of a defective bottle was held liable in negligence, and in a concurring opinion Justice Traynor states (p. 466):

“Warranties are not necessarily rights arising under a contract. An action on a warranty ‘was, in its origin, a pure action of tort,’ and only late in the historical development of warranties was an action in *assumpsit* allowed. (Ames, *The History of Assumpsit*, 2 Harv. L. Rev. 1, 8; 4 Williston on Contracts (1936) § 970.) ‘And it is still generally possible where a distinction of procedure is observed between actions of tort and of contract to frame the declaration for breach of warranty in tort.’ (Williston, *loc. cit.*; see Prosser, *Warranty On Merchantable Quality*, 27 Minn. L. Rev. 117, 118.)



“On the basis of the tort character of an action on a warranty, recovery has been allowed for *wrongful death* as it could not be in an action for breach of contract. (Greco v. S. S. Kresge Co., 277 N.Y. 26 (12 N.E. 2d 577, 115 A.L.R. 1020); see Schlick v. New York Dugan Bros., 175 Misc. 182 (22 N.Y. 2d 238); Prosser, op. cit., p. 119.) As the court said in Greco v. S. S. Kresge Co., supra, ‘*Though the action may be brought solely for the breach of the implied warranty, the breach is a wrongful act, a default, and, in its essential nature, a tort.*’ ” (Emphasis supplied.)

In *Automobile Ins. Co. v. Union Oil Co.*, supra, an action for damage to property, the Court held (pp. 303-304, 306-307):

“The first counts allege that on or about April 3 and 28, 1942, defendant sold to Aero Tool Company a product manufactured and prepared by the former for cleaning greasy and oily floors. That at the times of said sales defendant ‘*impliedly warranted \* \* \* that the said products or material was non-inflammable and was fit and safe for said use.*’ That said purchases were made in reliance upon such warranty. It is then alleged that the product was unfit and unsafe for use in cleaning greasy and oily floors in that the same was ‘highly inflammable and consequently dangerous.’ That ‘*as a proximate result of said breach of said implied warranty, a fire occurred at the plant of said Aero Tool Company \* \* \* on or about May 17, 1942, while the floors of said plant were being cleaned with said product or material by the regularly employed janitor of said Aero Tool Company and when said product*



came in contact with a lighted match which was being used by said janitor, who did not know of said inflammable nature of said product or material.'

"The second counts are the same as the first except that an express warranty of noninflammability is alleged rather than an implied warranty.

"The third counts allege the same facts as the first two, but set forth that defendant was guilty of negligence. \* \* \*

"Defendant answered the foregoing complaint, setting up, among other defenses, the bar of section 339, subdivision 1 of the Code of Civil Procedure.

"\* \* \* \* \*

"The sole question presented on this appeal is whether the complaint and the causes of action therein set forth are barred by the statute of limitations. \* \* \*

"\* \* \* \* \*

"Respondent urges that upon appellants' own theory of the case it falls within the provisions of section 339, subdivision 1 of the Code of Civil Procedure, which provides a two-year period. That the limitation period within which Aero Tool Company, the insured company, could have maintained an action against respondent is two years for the reason that under appellants' complaint, as to the insured, if any right of action at all is shown, it was only a right of action for breach of contract, which contract is oral and not evidenced by an instrument in writing. That the action is one 'ex contractu.' Appellants, on the

contrary, contend that the right of action on the part of the insured Aero Tool Company, to which appellants' claim is to be subrogated is 'ex delicto,' for the tortious injury to property and is controlled by subdivisions 2 and 3 of section 338 of the Code of Civil Procedure which provide a three-year period within which such an action may be commenced.

"In determining whether an action is on the contract or in tort, we deem it correct to say that it is the nature of the grievance rather than the form of the pleadings that determines the character of the action. If the complaint states a cause of action in tort, and it appears that this is the gravamen of the complaint, the nature of the action is not changed by allegations in regard to the existence of or breach of a contract. In other words, *it is the object of the action*, rather than the theory upon which recovery is sought that is controlling. (Gosling v. Nichols, 59 Cal. App. 2d 442, 444 (139 P. 2d 86); Lowe v. Ozmun, 137 Cal. 257, 259 (70 P. 87); Krebenios v. Lindauer, 175 Cal. 431, 433 (166 P. 17); Nathan v. Locke, 108 Cal. App. 158, 161, 162 (287 P. 550, 291 P. 286); Kings Laboratories v. Yucaipa Valley F. Co., 18 Cal. App. 2d 47, 49 (62 P. 2d 1054)).

"\* \* \* \* \*

"We are impressed that in the case now engaging our attention, the contract as pleaded had nothing whatever to do with the liability other than to create a duty on the part of respondent herein, and the action is grounded not upon the contract, but upon the duty springing from the relation created by it. While appellants might

have elected to sue either in tort or in contract, it clearly appears to us that the instant action *is based upon the injury done to property*. It, therefore, comes under the provisions of section 338 of the Code of Civil Procedure, which provides that the statutory period for commencing an action for injuring real property and goods and chattels is three years, and that, regardless of the theory upon which relief is sought, viz., whether on a negligence theory or a breach of warranty theory. In the case at bar the pleader was evidently following the commonly accepted practice of setting up the contract of warranty as a matter of inducement to show that a definite legal duty arose on the part of the respondent. *Where, as here, the breach of duty and consequent injury to one of the parties to such contract are set forth, it is the violation of its duty by respondent that is the gravamen of action, which accordingly sounds in tort and is not 'ex contractu'* (Basler v. Sacramento etc. Ry. Co., 166 Cal. 33, 35, 36 (134 P. 993))." (Emphasis supplied.)

It is apparent from these cases that appellant is gravely overstating the fact when she says, on page 26 of her brief, that: "In suits for a breach of warranty, both express and implied, the California Courts have uniformly applied the two-year statute."<sup>4</sup> The cases cited by appellant do not support the statement, and are not even relevant to the point made.

There is not a single California case applying anything but the one year statute to an action for personal injuries resulting from a breach of warranty.

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<sup>4</sup>Appellant's Opening Brief, page 26.

A better argument can be made where the personal injuries result from the breach of an express contract, but even this attempt has been made and rejected. In *Harding v. Liberty Hospital Corp.*, supra, the Court said (pp. 522-523):

“The appellants herein contend that the cause of action set forth in their complaint is one arising out of the breach of the plaintiff Margaret A. Harding’s contract with the defendant, such breach consisting in its failure to furnish adequate and competent surgical treatment for her injured limb, and hence that her cause of action being one for the breach of a written contract, does not come within the scope or effect of subdivision 3 of section 340 of the Code of Civil Procedure. Notwithstanding the elaboration with which the plaintiffs have undertaken to set forth the terms and provisions of their said contract, we are of the opinion that the *gravamen* of this action consists in the alleged negligent acts of the chief surgeon of the defendant, consisting in his unskillful setting of the said plaintiff’s injured limb, by reason solely of which the plaintiff’s alleged injury and damage arose. \* \* \* In that case this court held that the pleading of the contract by the plaintiffs was merely matter of inducement, out of the existence of which the definite legal duty of the defendant arose; and in that case, as in the instant one, the breach of that definite legal duty consisted in the alleged negligent acts and omissions of the agent of the defendant and consequent injury directly and solely caused thereby. The court there held that this was the gravamen of the action, citing numerous authorities in support of its view. In the later



case of *Krebenios v. Lindauer*, 175 Cal. 431 (166 Pac. 17), the same question arose and was similarly decided. There the injury complained of was the alleged negligence of the defendant in failing to provide the plaintiff with a safe place to work, in violation of its contract of employment, and the court there held the action to be one arising *ex delicto* and to be barred by the provision of the section and subdivision of the code above quoted. \* \* \* Notwithstanding the conflict of authority from other jurisdictions, we are satisfied that it has become the settled rule in California that actions for injuries caused by the negligent acts of another or his agent must be commenced within the period of one year from the date of the alleged injury, and that the fact that the parties stand in contractual relation to each other does not operate to change the rule or extend the time for the commencement of such actions."

The leading case on the point is *Basler v. Sacramento Electric Gas Ry. Co.*, *supra*, where suit was sought to be based upon a contract of safe carriage, and the Court said (pp. 36-37):

"It has been held that the word 'for' means 'by reason of,' 'because of' and 'on account of' and that a statute prescribing a limitation on 'actions for injury to the person \* \* \* caused by negligence' should be interpreted to mean 'actions "by reason of" or "because of" or "on account of" injuries to the person caused by negligence.' (*Sharkey v. Skilton*, 83 Conn. 503 (77 Atl. 950).) Applying this rule to our own statute *we must hold that the language of section 340 quoted above*



*refers to actions for damages 'on account of' personal injuries.* In *Sharkey v. Skilton*, the plaintiff was the husband of the injured woman and there, as here, counsel sought to make a distinction between the direct injury to the wife and the indirect damage and loss to the husband, but the court held that both harmful results had their efficient cause in the accident to her and that therefore the same statute of limitations applied to actions in which the wife was a party and to those in which the husband sued alone because of his relative rights.

“We see no escape from the reasoning of the foregoing authorities. The demurrer was properly sustained for the reason that the cause of action was pleaded as one arising *ex delicto*, but even if we should regard it as arising upon contract, nevertheless *the damages sought are directly referable to the personal injuries suffered by Mrs. Basler and consequently the time for the commencement of the action is limited by the terms of subdivision 3 of section 340 of the Code of Civil Procedure.*” (Emphasis supplied.)

We say, therefore, that appellant's action for personal injuries is clearly barred by the statute of limitations, and was properly dismissed.

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### CONCLUSION.

With respect to the action for wrongful death, appellant's case concededly depends upon a judicial determination that one provision of the Nevada statute

of limitations is not a part of the statute of limitations at all; but instead is an inherent, inseparable part of, and an express condition of and limitation upon, the wrongful death statute which is separated from it by sixty chapters, and which does not itself mention any time limitation. Appellant's argument is not reasonable. Further, the consequences of imposing such an absolute time limitation upon this statutory right are such that it should not lightly be done in the absence of a clear, legislative intent.

The Nevada statute of limitations could not more clearly be an ordinary, procedural limitation.

Apart from this, however, California law governs this case, and it is clear from the cases of *Gregory v. Southern Pacific Co.*, supra, and *Engel v. Davenport*, supra, that appellant could not avoid the bar of the one-year statute in the California Courts. In this connection, the *Engel* case states the only logical, proper rule, which is that even if the time limitation of the foreign statute is substantive, the only question that it affects is whether a cause of action can be stated; if it can, the next question is whether, procedurally, the California statute permits its enforcement. This question, together with matters of waiver of the statute, etc., are procedural things exclusively governed by the *lex fori*, in this case, the law of California.

Appellant's argument to sustain her action for personal injuries has been made to and refuted by the California Courts on numerous occasions.

Appellee respectfully submits that the District Court properly dismissed appellant's complaint, and that its order should be affirmed.

Dated, San Francisco, California,

May 12, 1950.

Respectfully submitted,

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No. 12,477

IN THE  
United States  
Court of Appeals

For the Ninth Circuit

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MARY ZELLMER, as Administratrix of the  
Estate of Orval Zellmer and MARY  
ZELLMER, an Individual,

*Appellant,*

VS.

ACME BREWING Co., a Corporation,

*Appellee.*

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Appellant's Closing Brief

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No. 12,477

IN THE

United States  
Court of Appeals

For the Ninth Circuit

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MARY ZELLMER, as Administratrix of the  
Estate of Orval Zellmer and MARY  
ZELLMER, an Individual,

*Appellant,*

vs.

ACME BREWING Co., a Corporation,

*Appellee.*

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**Appellant's Closing Brief**

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The Appellee's contentions are three in number (page 4, Brief for Appellee). These contentions will be answered in the order there set forth.

- 1. Appellee's First Contention That the Action for Wrongful Death Was Properly Dismissed Because the Nevada Time Limitation Is Procedural Only, Is Advanced by Appellee Without Supporting Authority.**

This contention rests almost entirely upon the case of *Gregory v. Southern Pacific Co.* (9th Cir. 1907), 157 Fed. 113. Appellee argues that: (1) The Nevada limitation is



identical to the limitation contained in California Code of Civil Procedure 340(3), and that (2) *Gregory v. Southern Pacific Co.*, *supra*, an Oregon Federal case has construed California Code of Civil Procedure 340(3) as procedural in nature, and that (3) this Court is therefore bound to hold that the Nevada limitation is procedural in nature.

Appellee's basic premise is erroneous. The California limitation considered in the *Gregory* case is significantly different from the Nevada limitation under consideration here, as is demonstrated by the *Gregory* case itself; and secondly, the nature of the Nevada limitation is a question to be answered by resort to Nevada law and the intent evidenced by the Nevada legislature in enacting the limitation. Since there are no Nevada decisions on this point, this Court is free to decide for itself the question as to what the Nevada legislature intended.

Moreover, *Gregory v. Southern Pacific Co.*, *supra*, far from supporting Appellee's contention, is in fact persuasive authority for Appellant's position. This was an action filed in Oregon for a death occurring in California. The action was filed more than one year after the death occurred, but within the time allowed by the Oregon limitation on wrongful death actions. Defendant demurred to the Complaint on the ground that the California time limitation had expired. Relying on the history of the statute, the Circuit Court of Appeals reversed the decision of the trial court which had sustained the demurrer.

The Court traced the history of the California statute emphasizing the fact that the cause of action for wrongful death had originally been enacted, together with the time limitation thereon, by the same statute in 1862 (St. Cal. 1862, p. 447, c. 330).

In 1872 the California legislature enacted the Code of Civil Procedure, and placed the time limitation on actions for wrongful death in Section 339 of the California Code of Civil Procedure grouping, by way of orderly classification, other statutes of limitation in the same chapter. In the form then adopted, the pertinent provisions of the California Code of Civil Procedure read as follows:

“335. The periods prescribed for the commencement of actions other than for the recovery of real property, are as follows:

‘339. Within Two Years.

4. An action to recover damages for the death of one caused by the wrongful act of another.’”

It was that form rather than the present form of the California limitation which was identical in almost all respects to the form of the Nevada limitation now under consideration.

That form of the limitation was left unchanged until 1905. In that year, the legislature amended sections 339 and 340 of the California Code of Civil Procedure (St. Cal. 1905, p. 231, c. 258). This amendment removed the limitation which had been found in Section 339(3), and inserted it in Section 340(3) of the California Code of Civil Procedure, shortening the time within which wrongful death actions could be filed, to one year.

Section 340(3) of the Code of Civil Procedure then read:

“340. Within One Year:

3. An action for libel, slander, assault, battery, false imprisonment, seduction, or for injury to or for the death of one caused by the wrongful action or neglect

of another, or by a depositor against a bank for the payment of a forged or raised check.”

This change was considered by the court in the *Gregory* case as a very significant one, in that it destroyed the limitation as one *which stood alone in a class by itself*, and lumped it together in a single subsection with the limitations applicable to seven other actions. The court states (at page 115 of 157 Fed.):

“Under this limitation were conjoined other actions, such as for libel, slander, and the like, *whereas the action for death through the wrongful act of another had formerly stood as a single cause in its own class.*\* It may be said that the change was brought about by simply dropping this cause of action out of section 339, prescribing the limitation of two years, *and inserting it, among other causes, in section 340, prescribing a limitation of but one year.*”

The court recognized the basic rule set forth in Appellant’s Opening Brief. That rule has been uniformly applied, and in fact its application was recently extended in the *Maki* and *Calvin* cases (see pp. 8-13 Appellant’s Opening Brief). In stating the rule, the court quoted from *Boyd v. Clark* with approval, saying (at page 116 of 167 Fed.):

“Reduced to a rule, the doctrine was stated by Mr. Justice Brown, late of the Supreme Court, while a District Judge, as follows:

‘That where a statute gives a right of action unknown to the common law, and either in a proviso to the section conferring the right, *or in a separate section*, limits the time within which an action shall be brought, such limitation is operative in any other jur-

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\*Emphasis supplied throughout unless otherwise indicated.

isdiction wherein the plaintiff may sue.' *Boyd v. Clark* (C.C.) 8 Fed. 849, 852."

It is clear that it was the 1905 amendment when considered with the prior history of the limitation, which compelled the court to decide that the nature of the limitation had been changed. The amendment of 1905 was, indeed, "the straw that broke the camel's back." The court stated (at page 119 of 157 Fed.):

*"The setting part of the limitations clause out of the old statute, the eradication of the idea of a proviso in relation to it, its arrangement under the ordinary statutes of limitations, along with the limitations as to the commencement of other actions and causes, and the subsequent treatment of the specific subject by transferring it from the limitation of two years and classifying it with the one-year limitation, is cumulatively so persuasive as to exclude the thought that it was to be still the purpose of the Legislature that the limitation should stand as a condition to exercising the right of action at all."*

A comparison of this limitation and its history with the Nevada limitation and its history shows that the Nevada legislature has evidenced a directly opposite intent. Appellee erroneously states throughout its argument that the Nevada limitation is identical to the California limitation considered by the *Gregory* case. Quite the contrary is true. The Nevada limitation is, however, identical in structure and arrangement to the California limitation *prior to 1905*.

The history of the Nevada cause of action and its limitation is as follows: The original cause of action for wrongful death was created in 1871 (St. Nev. 1871, p. 90). No specific limitation was established at that time. Instead,



the cause of action was controlled by a *general limitation* established in 1861, which did not mention a cause of action for wrongful death at all (St. Nev. 1816, p. 29). As the cause of action was originally created, therefore, the limitation was procedural in nature.

The *present* cause of action with which we are here concerned was enacted in 1911 as a part of the *present*<sup>1</sup> Civil Practice Act (Sts. Nev. 1911, Nev. Comp. Laws, Sec. 9194). In place of the former *general* limitation which had existed for the old cause of action, the legislature established, as a part of the same act, the present *specifically directed* limitation. The statutory history of the Nevada limitation is, accordingly, exactly the reverse of the California limitation.

Although our position is that, regardless of its history, the present form of the Nevada limitation is clearly such as to make it substantive in nature, the history of the limitation removes all doubt on this subject. The court in the *Gregory* case held the California limitation to be procedural because of its history of change in character from *specific to general*. It is clear, therefore, that the *Gregory* court would have held the Nevada limitation substantive because of its history of change in character from *general to specific*.

Appellee does not challenge the validity of the general rule that a time limitation on a cause of action for wrongful death is substantive in nature in either of two situations: (1) Where the limitation is contained in a proviso attached to, or incorporated in, the section of the statute

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1. There have been three Civil Practice Acts of Nevada (St. Nev. 1861, p. 314; St. Nev. 1869, p. 196, and the present Act of 1911).



creating the cause of action, and (2) where the limitation is contained in a different section of the same statute, but is directed specifically to the cause of action for wrongful death. Appellee merely seeks to abolish by its own argument, without support from judicial precedent, the second half of this well recognized rule.

Appellee concludes its argument on this point by stating (at page 12, Brief for Appellee):

“If appellant’s argument were at all sound, it would necessarily follow that *all* of the limitations periods of the Act were substantive, since they are in the ‘same Act’ as the actions to which they refer.”

It is a sufficient answer to such an argument to point out that the problem *arises* only with relation to those causes of action which were unknown to the common law, and which were created in the first instance by statute.

The balance of the authorities cited by Appellee provide no more support for its first contention that does the *Gregory* case. The first of these cases in *Anderson v. Linton* (7th Cir. 1949), 178 Fed. 2d 304 (at p. 7, Brief for Appellee). It is true that the Court held an Iowa statute of limitations to be procedural in nature. In doing so, however, it accepted and applied the general rule advanced by Appellant. The court stated (at page 310 of 178 Fed. 2d):

“Thus, if the original statute for wrongful death still existed in Iowa, and that statute contained a two-year period of limitation, the action could be brought within that period in the State of Illinois, *Coffman v. Wood*, D.C.N.D. Ill., 5 F. Supp. 906.”

The Iowa statute involved did not even faintly resemble the Nevada limitation here under consideration. The limi-

tation was construed as applying to actions for wrongful death although it did not even mention those actions. Section 614.1, Iowa Code, 1946, states:

“614.1 (3) *Injuries to person or reputation—relative rights—statute penalty—setting aside will.* Those founded on injuries to the person or reputation, including injuries to relative rights, whether based on contract or tort, or for a statute penalty, within two years; and those brought to set aside a will, within two years from the time the same is filed in the clerk’s office for probate and notice thereof is given, provided that after a will is probated the executor may cause personal service of an original notice to be made on any person interested, which shall contain the name of decedent, the date of his death, the court in which and the date on which the will was probated, together with a copy of said will; said notice shall be served in the same manner as original notices and no action shall be instituted by any person so served after one year from date of service.”

The next decision cited by Appellee (at p. 7, Brief for Appellee), is *Hughes v. Lucker* (3rd Cir., 1949), 174 Fed. 2d 285. This was a suit filed in the Federal court in Pennsylvania for a death occurring elsewhere. The decision does not purport to determine the question here at issue. The court merely pointed out that the Supreme Court of Pennsylvania had already decided the *exact* question, and that the Federal courts of Pennsylvania were therefore bound, without regard to what was thought of the wisdom of the Pennsylvania court’s decision. The case accordingly is no authority at all with regard to the instant problem since this Court is not bound by a prior decision of a California court, and is free to decide the question for itself.

The last case cited (at p. 7, Brief for Appellee) is *Keys v. Pullman Co.* (D.C., Tex., 1949) 87 Fed. Supp. 763. This was a suit for wrongful death filed in the Federal District Court in Texas for a death occurring in Pennsylvania. The Pennsylvania statute on actions for wrongful death (12 Purdons Penn. St., Sec. 1603) was as follows:

“Section 1603. Statement of parties to be made in declaration.

‘The declaration shall state who are the parties entitled in such action; *the action shall be brought within one year after the death, and not thereafter.*’ ”\*

The court stated (at page 765 of 872 Fed. Supp.):

“*The trend of decision and perhaps the weight of authority in the Federal Appellate Courts is that the above italicized wording in Section 1603 is not an ordinary Statute of Limitation, but that it conditions plaintiff’s right of action.* But I think the weight of authority in the Appellate Courts of Pennsylvania is that it is only an ordinary Statute of Limitation.”

The court was thus bound by Pennsylvania decisions construing the Pennsylvania statute as procedural only. The case offers no support for Appellee’s contention since there is no Nevada decision similarly construing the Nevada limitation here involved.

It can thus be seen that the first of Appellee’s contentions (p. 4, Brief for Appellee) is completely unsupported by authority. In contrast, Appellant’s position in this regard is amply supported by judicial precedent. Indeed, the *Maki* case and the *Calvin* case (pp. 8-11, Appellant’s Opening Brief) held limitations to be substantive in nature which were far *less* specifically directed to the causes of action limited than is the Nevada limitation. *Appellee cites*

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\*Court’s emphasis.

*no contrary authority whatsoever.* It merely asserts that those cases were in error and attempts to fill the gap with a statement of its own opinion.

## **2. Appellee's Second Contention Is Based on the Erroneous Assumption That a California Rule Has Been Established Which Is Binding on This Court.**

Appellee relies entirely on the case of *Engel v. Davenport* (1924) 194 Cal. 344, wherein the California Supreme Court attempted to apply sec. 340(3) of the California Code of Civil Procedure to a suit for personal injuries brought in California under the Employers Liability Act. Appellee concedes in a footnote (p. 16, Brief for Appellee) “\* \* \* that the *result* of this case was reversed in 271 U.S. 33, 70 L. Ed. 813, on the ground that this was not a case involving conflict of laws \* \* \*” and then produces its “of course” argument,<sup>2</sup> saying that “\* \* \* the case does, *of course*, state the California rule applicable to conflicting state laws, over which rule the U.S. Supreme Court has no authority.”

The fact that the case was reversed by the Supreme Court of the United States seems to trouble Appellee not at all. The very fact of its reversal should be a sufficient answer to Appellee's argument that it represents controlling authority.<sup>3</sup>

There are, however, other reasons why *Engel v. Davenport*, *supra*, does not control the decision of this Court. First of all, the action was for personal injuries, while the present action is for wrongful death. Since a cause of

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2. The “of course” argument defies classification. It is seemingly a device whereby one clothes one's own opinion with an appearance of authority when unable to find judicial precedent in point.

3. *Ruppert v. Ruppert* (App. D. C., 1943) 134 F.2d 497.



action for personal injuries existed at common law, the California limitation would have applied in the absence of a Federal statute *regardless* of rules of Conflict of Laws. In cases of wrongful death, however, the cause of action did not exist at common law, and a completely different principle governs the application of time limitations.

Secondly, the remarks of the Supreme Court in *Engel v. Davenport*, *supra*, were *obiter dicta*, and as such, are entitled to no weight in the instant case. The California court completely misconceived the legal issues involved in the *Engel* case, as is shown by the decision of the Supreme Court of the United States (*Engel v. Davenport* [1925] 271 U.S. 33, 46 S.C. 410, 70 L. Ed. 813), which reversed the decision of the California court. The case involved only the following questions: (1) Did the Employers Liability Act incorporate the two-year limitation on suits provided by the Merchant Marine Act? (the Employers Liability Act does not itself contain a statute of limitation); and (2) if so, could a state court disregard that limitation, and apply instead a limitation provided by a state statute?

The Supreme Court of California answered the first question negatively. In so doing, it disposed of the case. The Supreme Court of the United States held that the California court was wrong. Even had the California Supreme Court been correct in its holding, the problem here at issue could not have been involved since it is settled that where a Federal statute gives a cause of action without providing a limitation thereon, the limitation of the state where enforcement is sought will *always* be applied.<sup>4</sup>

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4. *Hanger v. Abbot* (1867) 73 U.S. 532; 6 Wall. 532; 18 L.Ed. 939; *Amy v. City of Dubuque* (1878) 98 U.S. 470, 25 L.Ed. 228;



The California court would have completely disposed of the case by its answer to the first question irrespective of whether its answer was in the affirmative or negative. After erroneously answering it in the negative, however, the court stated (at page 350 of 194 Cal.), "Conceding, however, for the sake of argument \* \* \*," and then proceeded with its dictum as to a Conflict of Laws rule. This situation is identical to that considered in the case of *Hargrove v. Henderson* (1930) 108 C.A. 667. The court, in discussing the effect of the case of *Peabody v. Phelps* ([1858] 9 Cal. 213) stated (at page 676 of 108 Cal. App.):

"The only question upon the point involved in the case of *Peabody v. Phelps* was whether or not an action for a false and fraudulent representation as to the naked fact of title in the vendor of real estate could be maintained by the purchaser \* \* \* and it was decided that such action would not lie but that the purchaser must bring his action for breach of the covenants in his deed. It is true that the learned justice who wrote the opinion in that case, *after thus concluding that the purchaser was restricted to an action for breach of the express warranties contained in his deed, took occasion to discuss, at considerable length, the question as to the right of a vendee who had taken a deed without express warranties of title, to maintain an action for fraud and deceit, and concluded that under such circumstances, such vendee would be without remedy, but, as heretofore noted, such question was not involved in the case, and the discussion of same in the opinion and the conclusion drawn may be regarded as pure dictum.\**

In view of this fact, we do not regard the decision in

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*Caldwell v. Alabama Dry Dock & Shipbuilding Co.* (5th Cir. 1947) 161 Fed.2d 83; cert. den. 68 S.Ct. 59, 332 U.S. 759, 92 L.Ed. 345; *Williamson v. Columbia Gas & Elect. Corp.* (3rd Cir., 1939) 110 Fed.2d 15; cert. den. 60 S.Ct. 1087, 310 U.S. 639, 84 L.Ed. 1407.

\*Court's emphasis.

the *Peabody v. Phelps* case as in any way controlling, nor even as authority in the case at bar.”

The case of *Childers v. Childers* (1946) 74 C.A.(2d) 56 also considers same point. The court stated (at page 61 of 71 C.A.(2d)):

“It is a fundamental rule of that doctrine (*stare decisis*) that a decision is not authority for what is *said*\* in the opinion but only for the points *actually involved*\* and actually decided. (*Norris v. Moody*, 84 Cal. 143, 149 (24 P. 37); *Hart v. Burnett*, 15 Cal. 530, 598.) The rule of *stare decisis* is a rule of public policy. For the preservation of harmony and for the stabilization of the law the courts will ordinarily follow precedents when the same points arise in subsequent litigation, although they will not persist in an absurdity or perpetuate a manifest error. There is no kinship between *stare decisis* and *obiter dictum*. Whatever may be said in an opinion *that is not necessary to a determination of the question involved is to be regarded as mere dictum*. (*Cardenas v. Miller*, 108 Cal. 250, 252 (39 P. 783, 41 P. 472, 49 Am. St. Rep. 84).) *The statement of a principle not necessary to the decision will not be regarded either as a part of the decision or as a precedent that is required by the rule of stare decisis to be followed.*”

Moreover it is settled that Federal courts do not follow dicta of state courts. (*DeLong v. Jefferson Standard Life Insurance Co.* [5th Cir. 1940] 109 Fed.2d 585; cert. den. in 60 S.Ct. 1081, 310 U.S. 635, 84 L.Ed. 1022; *New England Mutual Life Insurance Co. v. Mitchell* [4th Cir. 1941] 118 Fed.2d 414; cert. den. in 62 S.Ct. 60, 314 U.S. 629, 86 L.Ed. 505; 28 U.S.C.A. § 725).

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\*Court's emphasis.

In the *Mitchell* case, for example, the court stated (at page 420 of 118 Fed.2d) :

“In ascertaining the applicable law of the state, we are to consider court decisions and other available sources of local law; and we are to apply court decisions in the light of the well-established stare decisis rule and its limitations. Cf. *West v. American Tel. & Tel. Co.*, 61 S.Ct. 179, 85 L.Ed. .... We are not required, however, to speculate as to how the state court might decide the question before us if it has not already decided it. Nor should we *surrender our own judgment as to what the local law is on account of dicta* or other chance expressions of the judges of the local courts. The respectful attitude towards the local court, *where there has been no decision on the precise question before us*, is to consider that question in the light of the common law of the state, *with a view of reaching the decision which reason dictates, and with the faith that the local court will reach the same decision when the question comes before it*. To base a decision upon dicta, or upon *speculation as to what the local court might decide in the light of dicta*, would be to depart from our solemn duty in the premises and embark upon a vain and illusory enterprise.”

This court should similarly refuse to be influenced by a dictum expressed twenty-five years ago which is contrary to the rule followed by Federal courts.

The *Engel* case was reviewed in 13 California Law Review 411, and the fallacy of the court's reasoning on Conflict of Laws discussed. The author deplored the court's refusal to follow the “Federal rule” and concluded (at p. 414 of 13 Calif. Law Review) :

“The purpose of the statute of limitations is to prescribe a time within which to bring the action; this is

so whether the limitation and the right arise from one statutory enactment or whether they arise from separate unconnected enactments; *and the same is true whether the period prescribed by the statute, of the foreign jurisdiction, creating the right is shorter than the period prescribed by the law of the forum, or whether it is longer than such period.* Can it be said that it is any more in contravention of the policy of the forum, or any more inconvenient for its courts, to enforce the limitation in the one case than in the other? The practical result of the situation is that the court of the forum *gives the defendant all the defenses he could have had in the courts of the foreign jurisdiction, while it does not give the plaintiff all the advantages which he would have been given in those courts, and one of which is the privilege of bringing the action any time within the prescribed period. Neither the reasons for the general rule, as already outlined, nor any principle of law demand such a result as this.*"

Appellant does not dispute the fact that there are decisions in state courts, other than those of California, which refuse to apply the substantive time limitation of the *lex loci* when the law of the forum provides a shorter limitation. The better rule, however, is the one which Federal courts apply when not bound by state decisions. The annotation (68 A.L.R. 217) relied upon by Appellee (beginning p. 22, Brief for Appellee) itself points out this division among state decisions. Appellee merely quotes the writer's own personal views. Perhaps the latest and most complete collection of authorities on this point is set forth by the case of *Lewis v. Reconstruction Finance Corporation*, (App. D.C. 1949) 177 2d 654 (p. 17, Appellant's Opening Brief). The court recognized the two lines of au-



thority but in applying the rule contended for by Appellant, stated (at page 655 of 177 Fed. 2d) :

“In dealing with this conflict of authority, unaided by any decision of this court *directly in point*, we conclude that the limitation laid down by the law of the state where the fatal injuries occurred should govern, unless the public policy of the forum is clearly opposed. *We think this view is better supported by reason and authority.*”

### **3. Appellant Ignores the Question of Statutory Construction, Which Is the Only Question Involved in Appellant's Claim for Her Own Personal Injuries.**

A brief restatement of Appellant's position with regard to the statute of limitation applicable to a cause of action for personal injury resulting from breach of warranty seems therefore appropriate. In the first place, Appellant does not contend that the cause of action for personal injuries arising by reason of a breach of warranty is either *ex contractu* or *ex delicto*. Whether this cause of action is contractual or tortious in nature is simply immaterial. The question is one of statutory construction alone. Appellee does not dispute the fact that Section 339(1) of the California Code of Civil Procedure is the *general* statute of limitations in this state, and that it limits *both contractual and tortious* causes of action, so long as they are not removed from its scope by *specific provision* elsewhere.

Appellee's extensive arguments, which deal almost entirely with the question of whether or not the cause of action for Appellant's personal injuries is tortious or contractual in nature, are therefore immaterial.

Contrary to Appellee's assertion (page 28, Brief for Appellee), Appellant's contention has *never* been considered



by a California court. None of the cases cited by Appellee are applicable to this situation. The case of *Automobile Insurance Co. v. Union Oil Company* (1948) 85 C.A. 2d 302, does, however, deserve comment. The question there involved was whether or not a suit for property damage occurring by reason of defendant's breach of an implied warranty, was covered by California Code of Civil Procedure, Section 338(2), or by California Code of Civil Procedure, Section 339(1). The court held quite logically that the former section was applicable. California Code of Civil Procedure, Section 338 states:

“§ 338. Within three years:

2. An action for trespass upon or injury to real property.”

The contrast between this section and the limitations on personal injuries provided by California Code of Civil Procedure, Section 340(3) is highly significant. Whereas Section 338(2) covers *all* injuries to real property, without limitation, Section 340(3) covers those actions for personal injuries “\* \* \* caused by the wrongful act or neglect of another \* \* \*”. The difference in legislative intent is apparent. The limitation on actions for personal injuries contained in sec. 340(3) is very clearly limited to those produced in a specified manner, whereas the limitation on causes of action for damage to real property is not so limited. The *Automobile Insurance Company* case therefore is not authority for the proposition that the legislature intended, by the enactment of Section 340(3), to withdraw actions for personal injury arising without fault or neglect of the defendant, from the broad general scope of California Code of Civil Procedure, Section 339(1).

**CONCLUSION**

Appellee has failed to meet Appellant's arguments and authorities. In lieu of producing authorities to the contrary, Appellee has attempted to substantiate its otherwise unsupported arguments by devices such as its "of course" argument. We know that this Court will not be misled by such tactics and respectfully submit that justice will be done only by forcing Appellee to stand trial on the merits, both as to the claim for wrongful death, and as to the claim for Appellant's personal injuries.

Dated: San Francisco, Calif.,  
May 31, 1950.

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